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Too Big to Fail—Too Small to Compete: Systemic Risk Should be Addressed Through Antitrust Law but such a Solution will only Work if it is Applied on an International Basis

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TOO BIG TO FAIL – TOO SMALL TO COMPETE: SYSTEMIC RISK SHOULD BE ADDRESSED THROUGH ANTITRUST LAW BUT SUCH A SOLUTION WILL ONLY WORK IF IT IS APPLIED ON AN INTERNATIONAL BASIS

*Sharon E. Foster**

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I. INTRODUCTION

In March 2009 global stock markets, declining for five months, hit new lows. In the United States the Dow Jones Industrial average, S & P 500 and NASDAQ had fallen 54%, 56%, and 55%, respectively.[1] In the United Kingdom the FTSE was down 47%.[2] Markets in developing countries seemed to weather the storm better at first and there was talk that, perhaps, the dynamics of the global economy had changed with developing countries being decoupled or less dependent on good economic conditions in developed economies.[3] That proved not to be the case when markets in developing countries also began to fall.[4] Politicians in the United States tried to calm the panic by telling the people that the fundamentals of the domestic economy were sound.[5] The simple truth of the matter was that the fundamentals of the domestic economy were a mess, and this became evident when on

1. CNBC, Real Time Market Quotes, "Dow Jones Industrial Average Ndex," *available at* http://data.cnbc/quotes/DJIA/tab/2; CNBC Real Time Market Quotes, "S&P 500 Index," *available at* http://data.cnbc/quotes/.SPX/tab/2; CNBC, Real Time Market Quotes, "NASDAQ NMS Composite Index," *available at* http://data.cnbc.com/quotes/COMP/tab/1?viewtype=more.

2. CNBC, Real Time Market Quotes, "FTSE 100 Index," *available at* http://data.cnbc.com/quotes/GB;FTSE/tab/2.

3. *The Decoupling Debate: Emerging Markets*, ECONOMIST, Mar. 8, 2008, *available at* 2008 WLNR 4779950.

4. Jason Subler, *China Economic Data Surprises*, REUTERS, Sept. 11, 2009, http://www.nytimes.com/reuters/2009/09/11/business/business-uk-china.html; Randall S. Kroszner, Governor, Bd. of Governors of the U.S. Fed. Reserve Sys., Address at the Central Bank of Argentina 2008 Money and Banking Conference: The United States in the International Financial System: A Separate Reality? Resolving Two Puzzles in the International Accounts (Sept. 1, 2008), *available at* http://federalreserve.gov/newsevents/speech/kroszner20080901a.htm.

5. Alister Bull, *Bush Says Economic Fundamentals are Good*, REUTERS, Dec. 4, 2007, http://www.reuters.com/article/domesticNews/idUSWBT008021200712 04.

March 14, 2009 the U.S. government had to intervene to save the investment bank Bear Stearns, deemed too big to fail, from failing.[6]

Subsequently, the investment bank Lehman Brothers was allowed to fail and panic set in.[7] The markets continued to drop and it became apparent that there were numerous financial service firms in the United States and abroad that were teetering on the brink of failure.[8] Governments around the world intervened to save the too big to fail financial service firms due to concerns about systemic risk; the failure of one financial service firm causing the failure of others and, ultimately, unacceptable damages to the economy.[9] This government intervention took the form of government-backed mergers between weak financial service firms and stronger ones, an infusion of public funds into weak private financial services firms and government-sponsored entities on the verge of failure and special bankruptcy rules.[10] While this government intervention may have prevented the global financial services disaster from becoming worse, people around the world lost their life savings;[11] lost their jobs,[12] and lost their homes.[13]

How this financial crisis happened is still up for debate. On a very simplistic level we seem to have experienced market failure when there was no market for the "innovative" financial products, mostly securitized debt, created by the financial services sector. This created a credit freeze depriving financial service firms of short-term loans to

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6. Roddy Boyd, *The Last Days of Bear Stearns*, CNN MONEY, Mar. 31, 2009, http://money.cnn.com/2008/03/28/magazines/fortune/boyd_bear.fortune/.

7. Fang Wang et. al., *The End of Lehman Brothers*, FIN. TIMES, Sept. 15, 2008, http://www.ft.com/cms/s/0/2c0c5d82-8344-11dd-907e-000077b07658.html?nclick_check=1.

8. United Nations, World Economic Situation and Prospects 2009, http://www.un.org/esa/policy/wess/wesp2009files/wesp2009.pdf; Ben S. Bernanke, Chairman of the Bd. of Governors of the U.S. Fed. Reserve Sys., Speech at the National Association for Business Economics 50th Annual Meeting: Current Economic and Financial Conditions, (Oct. 7, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081007a.htm.

9. Fabia Panetta, et. al., *An Assessment of Financial Sector Rescue Programmes*, BIS PAPERS NO. 48, 10-19 (July 2009).

10. *Id.* at 10; Helen A. Garten, *Banking on the Market: Relying on Depositors to Control Bank Risks*, 4 YALE J. ON REG. 129, 146 (1986); *Corporate Bankruptcies in America: The Boom in Busts*, ECONOMIST, July 4, 2009, *available at* 2009 WLNR 12851000.

11. *See* Dow Jones, *supra* note 1; NASDAQ, *supra* note 1; S&P, *supra* note 1.

12. President Barack Obama, Remarks on the Economy (Jan. 28, 2009), *available at* http://www.whitehouse.gov/the_press_office/RemarksofPresidentBarackObamaontheEconomy; BUREAU OF LABOR STATISTICS, EMPLOYMENT SITUATION SUMMARY (2009), http://www.bls.gov/news.release/empsit.nr0.htm.

13. *Home Mortgages, Recent Performance of Nonprime Loans Highlights the Potential for Additional Foreclosures: Hearing Before the J. Economic Comm. of the United States Cong.*, 111th Cong. (2009) (statement of William B. Shear, Director, Financial Markets and Community Investment, U.S. Government Accountability Office).

service their debt, which far exceeded their assets.[14] In a free market, a firm that is not able to service its debt goes into bankruptcy or fails. But years of deregulation coupled with consolidation in the financial services sector due to a lack of antitrust enforcement resulted in mega financial service firms that pose systemic risk; that is, they are too big to fail.[15]

There are currently talks going on around the world about how to fix this problem. All focus on re-regulation of the financial services industry to manage systemic risk.[16] While such a move may be advisable,[17] we have seen in the past that, similar to the business cycle, there is a regulatory cycle where regulations are passed, enforced, reinterpreted, ignored, repealed and reenacted. Thus, regulations may provide some short term stability but as discussed below they do not eliminate the systemic risk inherent in too big to fail firms.

The only way systemic risk can be significantly reduced is to eliminate the too big to fail problem. That is where antitrust law may help to augment regulatory reform. Through Sherman § 2,[18] firms that are too big to fail and, thus, pose a systemic risk may face divestiture; the breaking up of a too big to fail firm into smaller firms that pose no such risk. Additionally, merger review under Clayton § 7[19] should utilize a systemic risk analysis and merger approval should be denied if such risk is probable.

That said, there are numerous problems to such an approach though most are of a practical nature. For example, as an economic and political reality, the United States cannot go the antitrust route alone, as there are firms outside the United States that pose systemic risks. Indeed, one reason U.S. financial services firms were allowed to become too big to fail was so they could compete with foreign firms

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14. Bernanke, *supra* note 8; BANK FOR INT'L SETTLEMENTS, QUARTERLY REVIEW (2008), http://www.bis.org/publ/qtrpdf/r_qt0912.pdf.

15. Albert A. Foer, *Preserving Competition After the Banking Meltdown*, GLOBAL COMPETITION POLICY, Dec. 15, 2008, https://www.competitionpolicyinternational.com/preserving-competition-after-the-banking-meltdown.

16. International Monetary Fund, About the IMF, June 2009, http://www.imf.org/external/about.htm; London Summit 2009, GROUP OF TWENTY, THE GLOBAL PLAN FOR RECOVERY AND REFORM (2009), http://www.g20.0rg/Documents/final-communique.pdf.

17. *But see* Stephen G. Breyer, *Anticipating Antitrust Centennial: Antitrust, Deregulation, and the Newly Liberated Marketplace*, 75 CAL. L. REV. 1005, 1007 (1987) (suggesting antitrust law may be preferable to regulatory law in a recently deregulated market).

18. 15 U.S.C. § 2 (2004).

19. 15 U.S.C. § 18 (1996).

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that were also too big to fail.[20] If, through divestiture and merger control, U.S. firms are no longer too big to fail they may be too small to compete. Accordingly, it is imperative that systemic risk analysis is integrated on a global basis to break-up and prevent the existence of too big to fail firms.

Part II of this Article provides some general definitions and some history of the regulatory cycle. Through this view of the recent past we can see the folly in relying solely on re-regulating the financial services sector. Regulations are prone to deregulatory cycles and the regulatory reform currently being discussed does not propose to eliminate systemic risk problems; it simply tries to manage them.

Part III describes the origins of the systemic risk problem to provide context for a systemic risk analysis. In this section, I also apply systemic risk analysis to Sherman § 2, Clayton § 7 and the antitrust rules articulated by the Supreme Court to show that such analysis will work under current law without the need for legislative amendment nor a reconsideration of the law by courts. While antitrust law in the United States seems to be in a constant state of flux, evolving to meet economic realities, systemic risk analysis does not require overturning precedent. Although antitrust enforcement by governmental agencies also seems cyclical in nature, private antitrust enforcement may eliminate this problem.

Finally, Part IV addresses the need for a global solution for systemic risk through harmonized antitrust laws; at least on the point of integrating systemic risk analysis in considering divestiture and merger issues. While, in the past, harmonization has not found favor for a variety of reasons, the global financial services meltdown certainly provides a motive and a starting point to reconsider this issue.

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20. Congressional Record (House) (May 13, 1998) H 3124, H3132-35, H3137-38, H3143; Congressional Record (House) (July 1, 1999 H5216-18, H5223, H5226-28, H5232, H5235-37, H5241, H5243-44; Congressional Record (House) (Nov. 4, 1999) H11519, H11522, H11525, H11527-28, H11536-36, H11544, H11547-48, H11550; Congressional Record (Senate) (May 5, 1999) S4742; Arthur E. Wilmarth, Jr., *The Transformation of the U.S. Financial Services Industry, 1975-2000: Competition, Consolidation, and Increased Risks*, 2002 U. ILL. L. REV. 215, 234-35 (2002); Sarah A. Wagman, *Laws Separating Commercial Banking and Securities Activities as an Impediment to Free Trade in Financial Services: A Comparative Study of Competitiveness in the International Market for Financial Services*, 15 MICH. J. INT'L L. 999, 1005 (1994).

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II. THE FINANCIAL SERVICES REGULATORY CYCLE: FROM REGULATION TO DE FACTO DEREGULATION TO DE JURE DEREGULATION AND BACK AGAIN

It is said that the definition of insanity is doing the same thing over and over again and expecting a different result.[21] If that is the case then we must ask if it is insane to think that re-regulation of the financial services sector will solve the problem of systemic risk. As with the business cycle of ups and downs we have seen a regulatory cycle of regulation – deregulation – re-regulation. There is no guarantee that we will not, yet again, de-regulate with giddy optimism of rational actors who are, in reality, acting with irrational exuberance causing the next fall into economic senseless despair. This section looks at the regulatory cycle, but first I shall provide some definitions for the sake of clarity.

A. *The Definitional Problem*

In researching just what happened to cause the financial crisis it became apparent that the complex nature of the investment transactions was not the only confusing aspect of this crisis. The interchangeability of terms relating to the institutions involved is a masterpiece of confusion. So, for ease of reference I shall define some terms here relating to the various financial service institutions involved. First, we have the term "commercial bank." Throughout this paper that term shall refer to banks that had a primary function, prior to legislative deregulation, of "acceptance of demand deposits from individuals, corporations, governmental agencies, and other banks; acceptance of time and savings deposits; estate and trust planning and trusteeship services; lock boxes and safety-deposit boxes; account reconciliation services; foreign department services (acceptances and letters of credit); correspondent services; investment advice."[22]

Next we have "savings & loans" also known as "thrifts." In this Article, the term "savings & loan" shall be used consistently throughout. Prior to deregulation, a savings & loan's primary function was the "safe-keeping of depositors' funds, with the resulting feature that both their deposits and investments were generally of a more permanent character than those of commercial banks."[23]

21. Albert Einstein, The Quotations Page, http://www.quotationspage.com/quote/Albert_Einstein/31.

22. United States v. Phila. Nat'l Bank, 374 U.S. 321, 327 (1963).

23. *In re* Wilkins' Will, 226 N.Y.S. 415, 425 (N.Y. 1928).

"Merchant banks" and "investment banks" are collectively defined as:

> [a]n individual or institution which acts as an underwriter or agent for corporations and municipalities issuing securities. Most also maintain broker/dealer operations, maintain markets for previously issued securities, and offer advisory services to investors. Investment banks also have a large role in facilitating mergers and acquisitions, private equity placements and corporate restructuring . . .[24]

The term "investment banks" shall be used consistently throughout this Article.

Then there is the "secondary banking sector" also known as the "shadow banking sector." This Article will use the term "shadow banking" which shall be defined as institutions, primarily investment banks, that provide unregulated financial services.[25] For example, in the United States a commercial bank is regulated by the Federal Reserve regarding deposits it takes in, but an investment bank, regulated by the Securities and Exchange Commission regarding the buying and selling of securities, is not regulated when it takes in deposits for money markets.[26]

Finally, there is the term "financial services." This term is used to describe the collective industry of commercial banking, investment banking and insurance.

B. *The Regulatory Cycle Begins*

In 1933, in response to the crash of the U.S. stock market in 1929 and subsequent bank failures, Congress passed the Glass-Steagall Act to restrict the ability of commercial banks to engage in investment banking.[27] The legislative history behind the Glass-Steagall Act indicates Congress believed that speculative investment by commercial banks was a major cause of commercial bank failures after the stock market crash and that the best way to avoid such problems in the future

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24. Investorwords, "investment bank," http://www.investorwords.com/2602/investment_bank.html (last visited Mar. 15, 2009); Investipedia, "merchant bank," http://www.investopedia.com/terms/m/merchantbank.asp (last visited Mar. 15, 2009).

25. Desi Franklin, *The Community Reinvestment Act: Subprime Crisis Villain, or Good and Misunderstood?*, 5 No. 16 ANDREWS BANKR. LITIG. REP. 9 (2008); Heidi Mandanis Schooner & Michael Taylor, *Convergence and Competition: The Case of Bank Regulation in Britain and the United States*, 20 MICH. J. INT'L L. 595, 623 (1999).

26. Paul S. Stevens & Craig S. Tyler, *Mutual Funds, Investment Advisers, and the National Securities Markets Improvement Act*, 52 BUS. LAW. 419, 421 (1997).

27. Wagman, *supra* note 20, at 1005.

was to separate commercial banking from investment banking.[28] While there has certainly been some dispute as to the cause of the bank failures in the 1930s[29] there is little room for doubt that banking regulation was passed in response to that economic crisis.[30]

From 1933 to around 1980, commercial bank expansion was limited by branching restrictions that prevented interstate banking; commercial bank competition for deposits was limited by caps on the amount of interest that could be charged and the type of business commercial banks could engage in was limited.[31] However, in the 1960s the shadow banking sector began offering higher interest rates in its unregulated money market accounts and commercial banks began losing customers.[32] To counter this loss of revenue, commercial banks increased consumer and mortgage lending.[33] However, this mechanism to increase revenue meant higher risk and diminished the overall quality of bank assets.[34] To further aggravate the situation, soaring oil prices during the 1970s led the Federal Reserve to drive up interest rates to control inflation which resulted in a higher costs for commercial banks and savings & loans to borrow money.[35] This caused the short-term cost of funding (the interest charged to commercial banks and savings & loans to borrow money) to be higher than the return on portfolios of mortgage loans (the interest commercial banks and savings & loans charged its customers on loans), a large proportion of which may have been fixed rate mortgages.[36] This problem is known as an asset-liability mismatch and was a principal cause the savings & loan crisis in the 1980s.[37] Additionally, the 1970s saw a marked increase in competition from foreign banks in the United States.[38]

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28. Inv. Co. Inst. v. Camp, 401 U.S. 617, 629 (1971).

29. *See* Benjamin J. Klebaner, AMERICAN COMMERCIAL BANKING: A HISTORY 138-48 (Twayne Publishers) (1990); George S. Eccles, THE POLITICS OF BANKING 81-86, 91-93 (Sidney Hyman ed., Graduate School of Business, University of Utah 1982).

30. Klebaner, *supra* note 29, at 142-47; Eccles, *supra* note 29, at 89-97.

31. Arthur F. Burns, THE ONGOING REVOLUTION IN AMERICAN BANKING 3-6 (1988); *see* Schooner & Taylor, *supra* note 25, at 621, 627.

32. Schooner & Taylor, *supra* note 25, at 623.

33. *Id.*

34. *Id.*

35. *Id.*

36. *Id.*

37. Zvi Bodie, *On Asset-Liability Matching and Federal Deposit and Pension Insurance*, ST. LOUIS FED. RESERVE, July/August 2006, http://research.stlouisfed.org/publications/review/06/07/Bodie.pdf.

38. Schooner & Taylor, *supra* note 25, at 623.

C. *The Beginning of the Deregulation Cycle*

In the United Kingdom during the 1970s, the Bank of England[39] responded to the growth of the shadow banking sector and the emerging presence of foreign institutions by deregulating domestic financial markets.[40] As a result of deregulation and loose fiscal and monetary policies, lending, particularly in the real estate sector, rose significantly.[41] When the real estate bubble in the United Kingdom burst, a number of institutions faced serious liquidity problems, and, as the crisis wore on, a growing number of them became insolvent.[42] The Bank of England, along with London and Scottish clearing banks, contributed resources to provide liquidity and bail out depositors of insolvent institutions.[43]

Back in the United States, commercial banks sought deregulation similar to that allowed in the United Kingdom in the 1970s in order to expand revenue opportunities by engaging in insurance and investment banking activities.[44] Additionally, U.S. commercial banks sought to curtail the competitive advantage of the growing number of foreign banks operating comparatively unregulated in the United States.[45] U.S. regulators were also anxious about the lack of supervision over foreign banks.[46] In response, Congress passed the International Banking Act of 1978 (IBA),[47] imposing domestic regulatory restrictions on foreign commercial banks.[48] The IBA was based on the principle of national treatment,[49] a concept familiar in international law. In effect, the IBA closed loopholes that had allowed foreign commercial banks operating in the United States to avoid the Glass-Steagall restrictions on investment banking activities and interstate banking limits imposed on U.S. commercial banks.[50]

The savings & loan crisis in the United States in the 1980s ushered in more deregulation in the United States. Because the sudden nature of

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39. The central bank for the United Kingdom serves a function similar to the U.S. Federal Reserve. *See* Bank of England website, http://www.bankofengland.co.uk (last visited Jan. 15, 2010).

40. Schooner & Taylor, *supra* note 25, at 624.

41. *Id.* at 625.

42. *Id.*

43. *Id.*

44. *Id.* at 627-28.

45. *Id.*

46. *Id.*

47. 12 U.S.C. §§ 3101-3108 (1988).

48. Bodie, *supra* note 37.

49. Craig M. Scheer, *The Second Banking Directive and Deposit Insurance in the European Union: Implications for U.S. Banks*, 28 GEO. WASH. J. INT'L L. & ECON. 171, 184-85 (1994).

50. Schooner & Taylor, *supra* note 25, at 627-28.

the inflation and the subsequent asset-liability mismatch threatened to cause hundreds of savings & loan failures, Congress partially deregulated the commercial banking and savings & loan industries.[51] It passed the Depository Institutions Deregulation and Monetary Control Act of 1980.[52] This Act phased out interest rate caps on commercial banks and savings & loans and authorized depository institutions nationwide.[53] It also allowed savings & loans to make consumer loans up to 20% of their assets, issue credit cards, accept negotiable order of withdrawal (NOW) accounts to enable them to compete for funding with the shadow banking sector,[54] and invest up to 20% of their assets in commercial real estate loans. Additionally, it allowed savings & loans to sell their mortgage loans and use the cash generated to seek better returns; the losses created by the sales were to be amortized over the life of the loan, and any losses could also be offset against taxes paid over the preceding 10 years.[55] This all made savings & loans eager to sell their loans. The buyers, major Wall Street firms, were quick to take advantage of the savings & loans' lack of expertise, buying at 60%-90% of value and then transforming the loans by bundling them as government-backed securities by virtue of government sponsored enterprises (Ginnie Mae, Freddie Mac, or Fannie Mae) guarantees.[56] Additionally, Congress passed the Garn-St. Germain Depository Institutions Act of 1982 which increased the proportion of assets that savings & loans could hold in consumer and commercial real estate loans and allowed savings & loans to invest 5% of their assets in commercial loans until January 1, 1984, when this percentage increased to 10%.[57]

Other changes in savings & loans oversight included authorizing the use of more lenient accounting rules to report their financial condition, and the elimination of restrictions on the minimum numbers of savings

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51. *See* H.R. REP. NO. 101-54(I) (1989) (Conf. Rep.); Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (1989); American Bar Association, *How a Good Idea Went Wrong: Deregulation and the Savings and Loan Crisis*, 47 ADMIN. L. REV. 643, 649 (1995).

52. American Bar Association, *supra* note 51, at 644.

53. *Id.* at 650.

54. H.R. REP. NO. 101-54(I), *supra* note 51.

55. Schooner & Taylor, *supra* note 25.

56. Carrie Stradley Lavargna, *Government-Sponsored Enterprises Are "Too Big to Fail": Balancing Public and Private Interests*, 44 HASTINGS L.J. 991, 997-99 (1993). GSE's are a federally charted, privately owned institution limited by their charters, granted by or pursuant to an act of Congress, to specific lending. *Accountability of Government Sponsored Enterprises: Hearing Before the J. Subcomm. on Capital Markets*, 105th Cong. 2 (1997) [hereinafter Stanton] (statement of Thomas H. Stanton); Scott Carnell, *Handling the Failure of a Government-Sponsored Enterprise*, 80 WASH. L. REV. 565, 570-72 (2005).

57. Schooner & Taylor, *supra* note 25, at 627.

& loans stockholders.[58] Such policies, combined with an overall decline in regulatory oversight, would later be cited as factors in the collapse of the savings & loans industry.[59]

The deregulation of savings & loans gave them many of the capabilities of commercial banks, without the same regulations. As savings & loan associations could choose to be under either a state or a federal charter, immediately after deregulation of the federally chartered savings & loans, state-chartered savings & loans rushed to become federally chartered in order to take advantage of the deregulation. Flushed with deregulated power, the savings & loans leaped at the chance to increase profit in the real estate boom of the late 1970s. Unfortunately, many savings & loans lent far more money than was prudent to risky ventures which many savings & loans were not qualified to assess. Further, what Congress gave through deregulation it took away through tax reform. The Tax Reform Act of 1986[60] removed tax shelters for real estate investments, significantly decreasing the value of many such investments which had been held more for their tax-advantaged status than for their inherent profitability. This, in turn, encouraged the holders of loss-generating properties to try and unload them, which contributed to the problem of sinking real estate values which contributed to the end of the real estate boom of the early to mid 1980s and further facilitated the savings & loans crisis.

D. *The De Facto Deregulatory Cycle*

Starting in the 1980s, a confluence of events led to regulatory agencies in the United States relaxing or ignoring regulatory requirements in the financial services sector.[61] While commercial banks and savings & loans were struggling in the 1970s and 1980s to find revenue generating avenues and to compete with foreign banks that could generate revenue through the stock markets and insurance markets, investment banks in the United States were also seeking new ways to generate revenue and compete with foreign investment banks that were not constrained with complex regulatory rules and limits.[62]

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58. *Id.* at 636.

59. *Id.*; S. REP. NO. 106-154, at S13896-97 (1999) (Conf. Rep.) (statements of Senator Dorgan); 1 FED. DEPOSIT INS. CORP., HISTORY OF THE EIGHTIES, LESSONS FOR THE FUTURE: AN EXAMINATION OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S (1997).

60. 26 U.S.C. § 469 (2005).

61. Wilmarth, *supra* note 20, at 250.

62. *See id.* at 234-35.

One mechanism to increase revenue with minimal regulatory oversight was through over the counter (OTC)[63] derivatives, primarily swap contracts.[64] Although swap contracts are "in the character of" futures contracts, and thus were under the regulatory purview of the Commodity Futures Trading Commission[65] (CFTC), the CFTC did not assert jurisdiction. Still, with the law on the books, the CFTC or a court could rule the swaps illegal if they did not conform to regulatory requirements rendering trillions of dollars in OTC derivative contracts unenforceable.

As with most financial debacles, the commercial banking and savings & loan crisis in the United States in the 1980s was not caused by one factor or one person. Rather, it was caused by a variety of factors and many people, most of whom were sitting in Congress and regulatory agencies. Commercial bank and savings & loan failures from 1980-1994 numbered around 1,300 or 1,600.[66] The debacle cost tax payers between $130 billion to over $1 trillion depending on teh set of "books at which one looks."[67] Considering the inadequate preparation for deregulation and the dire consequences thereof, it is rather surprising what Congress did next.

Attempts were made to deregulate the financial services sector in 1984, 1988, 1991 and 1995, but each attempt at de jure deregulation failed.[68] Unsatisfied with the slow, plodding nature of Congress and concerned with foreign competition, the Federal Reserve Board (Board), reinterpreted Section 20 of the Glass-Steagall Act and allowed commercial banks to do up to 5% of gross revenues from underwriting activities previously only allowed to be done by investment banks. Then, again in the spring of 1987, the Board allowed commercial banks to do more investment banking business over the objections of

63. Over the counter markets are transactions between parties and not through an exchange. Investopedia, http://www.investopedia.com/terms/o/over-the-countermarket.asp (last visited Nov. 14, 2009).

64. THE PRESIDENT'S WORKING GROUP ON FIN. MKTS., OVER THE COUNTER DERIVATIVES MARKETS AND THE COMMODITY EXCHANGE ACT 4-5 (Nov. 1999); Dorit Samuel, *The Subprime Mortgage Crisis: Will New Regulations Help Avoid Future Financial Debacles?*, 2 ALB. GOV'T L. REV. 217, 232-37 (2009).

65. Commodity Exchange Act, 7 U.S.C. § 2 (2008).

66. FDIC, *supra* note 59; Schooner, *supra* note 25, at 636.

67. Carl Felsenfeld, *Financial Institutions and Regulations, the S&L Crisis: Death and Transfiguration Symposium, The Savings and Loan Crisis*, 59 FORDHAM L. REV. S7, S29 n.144 (1991).

68. The Glass-Steagall Act, enacted in 1933, prohibited commercial banks from activities considered too speculative such as underwriting and dealing with securities (investment banking activities). Michael S. Raab, *The Transparency Theory: An Alternative Approach to Glass-Steagall Issues*, 97 YALE L.J. 603 (1988).

Chairman Paul Volker.[69] Alan Greenspan became the Chairman of the Federal Reserve Board in August, 1987.[70] Under Greenspan, the Board continued to deregulate the financial services sector allowing commercial banks to do more investment banking business.[71]

As a result of the savings & loan debacle, Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, (FIRREA) which changed the savings & loan industry and its regulatory structure.[72] Briefly, the Office of Thrift Supervision (OTS), a bureau of the Treasury Department, was created to charter, regulate, examine, and supervise savings institutions.[73] Additionally, FIRREA gave both Freddie Mac and Fannie Mae additional responsibility to support mortgages for low- and moderate-income families.[74] In 1991, Congress also enacted the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) in response to banking problems experienced in the 1980s.[75] This law established a new level of banking supervision, based on the level of capital, where regulatory agencies could take more severe action as capital levels decrease and was in accordance with the international Basel Capital Accord agreement.[76]

E. *More Foreign Deregulation – The European Union's Second Banking Directive*

The European Union passed the Second Council Directive of December 15, 1989 (the Second Banking Directive), which member

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69. DAVID ELY & KENNETH ROBINSON, FEDERAL RESERVE BANK OF DALLAS, FINANCIAL INDUSTRY STUDIES: HOW MIGHT FINANCIAL INSTITUTIONS REACT TO GLASS-STEAGALL REPEAL? EVIDENCE FROM THE STOCK MARKET 3 (1998), http://www.dallasfed.org/banking/fis/fis9801.pdf; Schooner & Taylor, *supra* note 25, at 644-46. Citicorp, 73 FED. RES. BULL. 473 (1987). Sec. Indus. Ass'n v. Bd. of Gov. of the Fed. Reserve Sys., 839 F.2d 47, 50 (2d Cir. 1988). "Thomas Theobald, then vice chairman of Citicorp, argued that three "outside checks" on corporate misbehavior had emerged since 1933: "a very effective" SEC; knowledgeable investors, and 'very sophisticated' rating agencies." Leonard J. Kennedy & Heather A. Purcell, *Wandering Along the Road to Competition and Convergence--The Changing CMRS Roadmap*, 56 FED. COMM. L.J. 489, 547 n.266 (2004). In the current economic crisis, all three of these "outside checks" have proven to be fatally defective. Jacob M. Schlesinger, *What's Wrong? The Deregulators*, WALL ST. J., Oct. 17, 2002, at A1.

70. Nathaniel C. Nash, *Greenspan Says He'd Sit Out Some Federal Reserve Votes*, N.Y. TIMES, July 11, 1987, http://www.nytimes.com/1987/07/11/us/greenspan-says–he-d-sit-out-some-federal-reserve-votes.html. Greenspan had formerly been a director of J. P. Morgan. *Id.*

71. J.P. Morgan & Co., 75 FED. RES. BULL. 192, (1989); Ely & Robinson, *supra* note 69, at 3.

72. Schooner & Taylor, *supra* note 25, at 637.

73. *Id.*

74. *Id.*

75. Practising Law Institute, *Capital Adquacy Ratio (CAR) in the Real World*, 7 NO. 21 P.L.I. POCKET MBA 1 (June 3, 2009); 12 U.S.C. § 1817 (2009); 12 U.S.C. § 1831 (2009).

76. 12 U.S.C. § 1817 (2009).

states were required to implement by January 1, 1993.[77] The directive established a single license applicable throughout the European Union for the provision of banking and other financial services. Thus, a credit institution[78] was able to provide a wide variety of financial services throughout the European Union.[79] These services include: acceptance of deposits from the public, lending, trading transferable securities, money market instruments, options and futures, foreign exchange and exchange and interest rate instruments, providing investment and financial advisory services, participating in stock issues and providing services related to such issues.[80] In essence, European Union banks could do commercial banking, investment banking and insurance business.[81]

The Second Banking Directive was not intended to merely have an effect in the European Union; it was intended, by design, to pressure non-European Union countries to reform their financial services laws so European Union financial services firms would have complete market access.[82] This was done through the comparable treatment requirement.[83] Under the comparable treatment requirement, a third country whose banks participate in the European Union's banking market must provide European Union banks with "effective market access comparable to that granted by the [Union] to credit institutions from that third country."[84] If it appeared to the Commission that a third country was not giving European Union banks comparable treatment, the Commission could submit proposals to the European Union Council for authority to negotiate with that third country.[85] Thus, if European Union banks were not allowed in a foreign country to do everything they were allowed to do in the European Union, punitive action was possible.[86] Prior to the repeal of Glass-Steagall by the Financial Services Modernization Act in 2000, the only way the United States

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77. Second Council Directive, *infra* note 79.

78. A "credit institution" is an undertaking "whose business is to receive deposits or other repayable funds from the public and to grant credits for its own account." First Council Directive 77/780, art. 1, 1977 O.J. (L 322) (EEC) (as amended by Council Directive 86/524, 1986 O.J. (L 309) (EEC)).

79. Second Council Directive 89/646, pmbl., Annex, art. 18, 1989 O.J. (L 386) (EEC); HAROLD S. BLOOMENTHAL & SAMUEL WOLFF, SECURITIES AND FEDERAL CORPORATE LAW § 27:75 (2d ed.) (Mar. 2009).

80. Second Council Directive, *supra* note 79, pmbl., Annex, art. 18.

81. *Id.*

82. Craig M. Scheer, *The Second Banking Directive and Deposit Insurance in the European Union: Implications for U.S. Banks*, 28 GEO. WASH. J. INT'L L. & ECON. 171, 177-78 (1994).

83. *Id.*

84. *Id.*

85. *Id.*; Second Council Directive 89/646, art. 9, ¶¶ 3 & 4, 1989 O.J. (L 386) (EEC).

86. Scheer, *supra* note 82; Second Council Directive 89/646, art. 9, ¶¶ 3 & 4, 1989 O.J. (L 386) (EEC).

could provide European Union banks with comparable treatment was to liberalize its banking laws to the same extent as the Second Banking Directive.[87] If this was not accomplished the European Union could decide to not allow U.S. financial service firms access to the European Union market.

F. *De Facto Deregulation Accelerates in the United States*

After the Second Banking Directive passed in the European Union, there was an acceleration of deregulation in the United States. In 1989, the CFTC issued the Swap Policy Statement, which reflected the agency's view that "most swap transactions, although possessing elements of futures or options contracts are not appropriately regulated as such under the Act [CEA[88]] and regulations."[89] This statement was issued to ease concern about the legality of certain derivative contracts but the CFTC at the time lacked authority to exempt futures contracts from the provisions of the CEA that required all such contracts to be traded on contract markets approved by the CFTC in order to be legal.[90] Accordingly, the legal certainty of derivative contracts was an issue.

In 1990, J.P. Morgan became the first commercial bank to receive permission from the Board to underwrite securities, so long as its investment banking business did not exceed the 10% limit. This de facto deregulation was followed by de jure deregulation with the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994[91] which repealed the 1927 McFadden Act provision limiting interstate banking, and part of the Bank Holding Company Act of 1956 restricting purchase by one commercial bank of a commercial bank in another state.[92]

In 1995 Fannie Mae and Freddie Mac began receiving government incentive payments for purchasing mortgage backed securities.[93] Thus began the involvement of the government-sponsored entities (GSE)

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87. Scheer, *supra* note 82, at 201; George S. Zavvos, *Banking Integration and 1992: Legal Issues and Policy Implications*, 31 HARV. INT'L L.J. 463, 496 (1990).

88. Commodity Exchange Act, 7 U.S.C. §§ 1-27(f) (1922).

89. COMMODITY FUTURES TRADING COMM'N, POLICY STATEMENT CONCERNING SWAP TRANSACTIONS 30694 (1989), *available at* 1989 WL 278866.

90. *See* THE PRESIDENT'S WORKING GROUP ON FIN. MKTS., OVER-THE-COUNTER DERIVATIVES MARKETS AND THE COMMODITY EXCHANGE ACT 6-9 (1999). Such authority was provided in a limited extent under the Futures Trading Practices Act of 1992.

91. Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, Pub. L. No. 103-328, § 1(a), 108 Stat. 2338 (1994).

92. Schooner & Taylor, *supra* note 25, at 643-44.

93. Carol D. Leonnig, *How HUD Mortgage Policy Fed The Crisis*, WASH. POST, June 10, 2008, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2008/06/09/AR2008060902626.html.

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with the subprime market.[94] Subprime mortgage originations rose by 25% per year between 1994 and 2003, resulting in a nearly 10-fold increase in the volume of subprime mortgages in just nine years.[95] The relatively high yields on these securities, in a time of low interest rates, were very attractive to Wall Street, and while Fannie and Freddie generally bought only the least risky subprime mortgages, these purchases encouraged the entire subprime market.[96]

Because of their government connections, investors believed that the government would not let a GSE fail. This enabled GSEs to leverage at a rate higher than other financial service institutions and they did.[97] From 2002 to 2006 Fannie Mae and Freddie Mac combined purchases of subprime securities rose from $38 billion to around $175 billion per year before dropping to $90 billion. During this time, the total market for subprime securities rose from $172 billion to nearly $500 billion only to fall back down to $450 billion.[98]

In December 1996, with the support of Chairman Alan Greenspan, the Board issued a precedent-shattering decision permitting commercial banks to own investment bank affiliates with up to 25% of their business in investment banking (up from 10%).[99] This expansion of the Board's 1987 reinterpretation of Section 20 of Glass-Steagall effectively rendered Glass-Steagall obsolete. However, because Glass-Steagall remained on the books there was some legal uncertainty.

In August 1997, the Board eliminated many restrictions imposed on "Section 20 subsidiaries" by the 1987 and 1989 orders. The stated justification for this deregulatory move was that the risks of underwriting had proven to be "manageable."[100] In 1997, Bankers Trust bought the investment bank Alex Brown & Co., becoming the first U.S. commercial bank to acquire an investment bank.[101]

In the fall of 1997, Travelers Insurance Company acquired the

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94. Subprime lending (near-prime, non-prime, or second chance lending) is a financial term that was popularized by the media during the "credit crunch" of 2007 and involves financial institutions lending to borrowers who do not meet prime underwriting guidelines.

95. Cynthia Angell & Norman Williams, *U.S. Home Prices: Does Bust Always Follow Boom?* (2005), http://www.fdic.gov/bank/analytical/fyi/2005/021005fyi.html.

96. Russell Roberts, *How Government Stoked the Mania*, WALL ST. J., Oct. 3, 2008, *available at* http://online.wsj.com/article/SB122298982558700341.html.

97. Scott Carnell, *Handling the Failure of a Government-Sponsored Enterprise*, 80 WASH. L. REV. 565, 570-72 (2005).

98. *Id.*

99. Schooner & Taylor, *supra* note 25, at 645; 61 FED. RES. BULL. 68, at 750 (1996); Bank Holding Companies and Change in Bank Control, 62 Fed. Reg. 2622-32 (proposed Jan. 17, 1997).

100. Bank Holding Companies and Changes in Bank Control, 62 Fed. Reg. 45,295 (1997) (to be codified at 12 C.F.R. pt. 225).

101. *Financial Restructuring: Hearing Before the H. Comm. on Banking and Financial Services*, 105th Cong. (1997) (statement of the Independent Bankers Association of America).

Salomon Brothers investment bank for more than $9 billion in stock.[102] This acquisition was justified as giving Travelers the wealth necessary to compete overseas.[103] On April 6, 1998, Travelers and Citicorp announced a $70 billion stock swap merging Travelers and Citicorp (the parent of Citibank), to create Citigroup, Inc., then the world's largest financial services company, in what was the biggest corporate merger in history.[104]

The Board gave its approval to the Citicorp-Travelers merger on September 23, 1998.[105] The Board's press release indicated that "the Board's approval [was] subject to the condition that Travelers and the combined organization, Citigroup, Inc., take all actions necessary to conform the activities and investments of Travelers and all its subsidiaries to the requirements of the Bank Holding Company Act in a manner acceptable to the Board, including by divestiture as necessary, within two years of consummation of the proposal."[106] The Board's approval was also subject to the condition that Travelers and Citigroup conform the activities of its companies to the requirements of the Glass-Steagall Act.[107]

G. *De Jure Deregulation*

In May 1998, the House passed legislation by a vote of 214 to 213 that allowed for the merging of commercial banks, investment banks, and insurance companies into huge financial conglomerates.[108] In September, the Senate Banking Committee voted 16-2 to approve a compromise bank overhaul bill.[109] Then, after 12 attempts in 25 years, and incremental de facto deregulation, Congress repealed Glass-Steagall and the Bank Holding Company Act of 1956 with the Financial Services Modernization Act of 2000 (FSMA), formerly known as the Financial Services Competition Act of 1997.[110] Financial service firms

102. Peter Truell, *A Wall Street Behemoth: The Deal; Travelers to Buy Salomon, Making a Wall St. Giant*, N.Y. TIMES, Sept. 25, 1997, *available at* http://www.nytimes.com/1997/09/25/business/a-wall-street-behemoth-the-deal-travelers-to-buy-salomon-making-a-wall-st-giant.html?pagewanted=1.

103. *Id.*

104. Schooner & Taylor, *supra* note 25, at 645 n.235.

105. *Id.*; Press Release, Bd. of Governors of the Fed. Reserve Sys., Order Approving Formation of a Bank Holding Company, and Notice to Engage in Nonbanking Activities (Sept. 23, 1998) (available in LEXIS, Federal Legal-U.S./Administrative Agency Materials/Individual Agencies File) [hereinafter Bd. of Governors of the Fed. Reserve Sys.].

106. Bd. of Governors of the Fed. Reserve Sys., *supra* note 105.

107. *Id.*

108. 144 CONG. REC. H3201-H3222 (1998).

109. Senate Banking, Housing and Urban Affairs Committee, Committee Documents, http://banking.senate.gov/docs/reports/hr10/hr10rpt.htm (last visited Apr. 2, 2010).

110. 144 CONG. REC. E1054-E1056 (1998); BD. OF GOVERNORS OF THE FED. RESERVE SYS.,

in the United States were now allowed to do what their European Union brethren were allowed to do under the Second Banking Directive.[111] The main goal of the legislation was to repeal the provisions of the Glass Steagall Act that restricted commercial banks and investment banks from affiliating so they could compete globally.[112]

But de jure deregulation was not complete in the United States. In November, 1999 the President's Working Group recommended the deregulation of the derivatives market based upon the legal uncertainty of the law.[113] In June, 2000 then Secretary of the Treasury Lawrence Summers testified before joint Senate committees on Agriculture, Nutrition, and Forestry and Banking, Housing and Urban Affairs that there was a need for legal certainty for derivative contracts; that U.S. markets were outdated compared to European Union markets; that certain derivatives should be excluded from regulatory oversight; and that the United States needs deregulation to be competitive.[114] Shortly thereafter the Commodities Futures Modernization Act (CFMA) was passed by Congress[115] and signed into law excluding derivatives from regulatory oversight.[116]

H. *The Financial Crisis Starting in 2007 Leads to Re-Regulation*

What ensued following the de jure deregulation in the United States was about four years of growth in the financial services sector followed by what some have called a total meltdown of the global credit markets and the nearest thing we have seen to the Great Depression.[117] What is

86TH ANNUAL REPORT 118 (1999).

111. *See* 145 CONG. REC. H5322-H5323 (1999); 145 CONG. REC. S13883-S13917 (1999).

112. *See* Jennifer Manvell Jeannot, *Note and Comment: An International Perspective on Domestic Banking Reform: Could the European Union's Second Banking Directive Revolutionize the Way the United States Regulates its own Financial Services Industry?*, 14 AM. U. INT'L L.R. 1715, 1739-40 (1999); *see generally* Financial Services Competitiveness Act of 1997, H.R. 10, 105th Cong. (1998) (The Bill's synopsis is "to enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, and other financial service providers, and for other purposes.").

113. THE PRESIDENT'S WORKING GROUP ON FIN. MKTS., OVER-THE-COUNTER DERIVATIVES MARKETS AND THE COMMODITY EXCHANGE ACT (1999), http://www.ustreas.gov/press/release/reports/otcact.pdf (last visited Apr. 12, 2010).

114. Press Release, U.S. Dep't of the Treasury, Treasury Secretary Lawrence H. Summers Testimony Before the Joint Senate Committees on Agriculture, Nutrition, and Forestry and Banking, Housing and Urban Affairs (June 21, 2000), *available at* http://www.treas.gov.oress/releases/ls722.htm.

115. 145 CONG. REC. H12502 (1999); 146 CONG. REC. S11885 (1999).

116. Dean Kloner, *The Commodity Futures Modernization Act of 2000*, 29 SEC. REG. L.J. 286, 290 (2001); BD. OF GOVERNORS OF THE FED. RESERVE SYS. ET.AL., JOINT REPORT ON RETAIL SWAPS: AS REQUIRED BY SECTION 105(C) OF THE COMMODITY FUTURES MODERNIZATION ACT OF 2000 1-2 (2001), *available at* http://www.ustreas.gov/press/releases/docs/rssfinal.pdf.

117. Stephen Labaton, *Agency's '04 Rule Let Banks Pile Up New Debt, and Risk*, N.Y.

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truly surprising is not that this happened but that so many "experts" did not see it coming. There were certainly enough voices of concern raised before the fall for those involved in the government and financial services sector to understand the vulnerabilities and avoid the meltdown. For example, when the FSMA was being debated in Congress, Representative John Dingell reminded the House of the dire repercussions the last time Congress deregulated (the savings & loan industry) and feared this would happen again with rampant speculation ending in a public bail-out.[118] Further, there were examples of housing bubbles and deregulatory chaos in other foreign markets.[119] Congress flew past these concerns and the financial services market did soar ever higher but only for a short time; ultimately financial service institutions fell back to earth creating harm and havoc on their way down.

The causes of the crisis are numerous: financial service firms were over leveraged,[120] poor risk analysis regarding debts and assets,[121] lack of regulatory oversight,[122] greed,[123] and hubris.[124] As with the Great

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TIMES, Oct. 3, 2008, at A1, *available at* www.nytimes.com/2008/10/03/business/03sec.html?em.

118. 145 CONG. REC. H5219 (1999). Rep. Dingell stated:

> It looks like this Congress is setting out to create exactly the same situation which caused the 1929 crash . . . Congress is setting out to create the situation that caused the collapse of the banks in Japan and Thailand by setting up . . . monstrous conglomerates which will expose the American taxpayers and American investors to all manner of mischief and to the most assured economic calamity . . . . First of all, it allows megamergers to create monstrous institutions which could engage in almost any sort of financial action. It sets up essentially, devices like the banks in Japan, which are in a state of collapse at this time, banks in Korea and Thailand, which are in a state of collapse, or banks in the United States, which could do anything and which did anything and contributed in a massive way to the economic collapse of this country in 1929 which was only cleared and cured by World War II.

119. *See generally* Basel Comm. on Banking Supervision, *Bank Failures in Mature Economies* (Bank for Int'l Settlements Working Paper No. 13, 2004), *available at* http://www.bis.org/publ/bcbs_wp13.pdf.

120. INT'L MONETARY FUND, ANNUAL REPORT 9 (2009), *available at* http://www.imf.org/external/pubs/ft/ar/2009/eng/pdf/ar09_eng.pdf.

121. BANK FOR INT'L SETTLEMENTS, BIS QUARTERLY REVIEW: INTERNATIONAL BANKING AND FINANCIAL MARKET DEVELOPMENTS 5 (2008), *available at* http://www.bis/org/publ/qtrpdf/r_qt0809.htm; Edward Carr, *In Plato's Cave*, ECONOMIST, Jan. 24, 2009, at 13.

122. Press Release, Comm. on Capital Mkts. Regulation, Recommendations for Reorganizing U.S. Regulatory Structure (Jan. 14, 2009), *available at* http://www.capmktsreg.org/press.html.

123. Aaron Unterman, *Innovative Destruction – Structured Finance and Credit Market Reform in the Bubble Era*, 5 HASTINGS BUS. L.J. 53, 54 (2009).

124. *See generally* Paul Krugman, *How Did the Economists Get it so Wrong?*, N.Y. TIMES, Sept. 6, 2009, at MM 36.

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Depression people are again calling for regulatory oversight of the financial services sector to avoid the excesses and speculation of an unregulated financial services industry.[125] So we go into another cycle of regulation; but what happens when we yet again go into the deregulatory cycle? Will we again ignore past experiences with deregulation and be doomed to repeat our mistakes? Probably, but one thing we can do is minimize the damage and one way to do that is through antitrust actions to divest the too big to fail firms into smaller firms for which failure is acceptable.

III. THE ANTIDOTE TO TOO BIG TO FAIL IS ANTITRUST

As a preliminary matter it must be said that the financial services sector is not exempt from antitrust laws. More critically, however, is that there is nothing in antitrust statutory law nor case law that would prevent the use of systemic risk analysis for purposes of divesting a firm that is too big to fail or preventing a merger. Antitrust has always been available as an antidote for too big to fail through divestiture and merger review; however, some believe that antitrust law would have to be reformed before it is applicable.[126] That is simply not the case.

A. *Financial Service Firms are not Exempt from Antitrust Laws*

Antitrust law is clearly applicable to commercial banking.[127] Investment banking may have a partial, implied exemption because of: "(1) the existence of regulatory authority under the securities law to supervise the activities in question; (2) evidence that the responsible regulatory entities exercise that authority; and (3) a resulting risk that the securities and antitrust laws, if both applicable, would produce conflicting guidance, requirements, duties, privileges, or standards of conduct."[128] This does not appear to pose a problem for Sherman § 2 nor Clayton § 7 application to systemic risk.

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125. *See* U.S. Department of State, "London Summit Communiqué: Global Plan for Recovery and Reform," *available at* http://www.pittsburghsummit.gov/resources/125131.htm; *see also* President Barack Obama, Remarks on 21st Century Financial Regulatory Reform (June 17, 2009), *available at* http://www.whitehouse.gov/the_press_office/Remarks-of-the-President-on-Regulatory-Reform/ [hereinafter Obama Remarks].

126. Albert A. Foer, *Preserving Competition After the Banking Meltdown*, GCP – THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY, Dec. 2008, at 6-7; *see generally* Daniel J. Mahoney, *"When Bank Mergers Meet Antitrust Law, There's No Competition." Why Antitrust Law Will Do Little to Prevent Overconsolidation Within the Banking Industry*, 14 ANN. REV. BANKING L. 303, 305 (1995).

127. *See, e.g.*, United States v. Phila. Nat'l Bank, 374 U.S. 321 (1963).

128. Credit Suisse Sec. (USA) LLC v. Billing, 551 U.S. 264, 275-76 (2007).

With respect to insurance, there is an express federal exemption for the "business of insurance" if it is also "regulated by State law."[129] So, to the extent a firm is engaged in all three financial services, it can be sued for antitrust violations regarding its commercial and investment banking businesses but there may be an exemption from antitrust law regarding its "business of insurance" that is regulated by State law.

B. *The Origins of Too Big to Fail*

The too big to fail doctrine seems to have first been articulated in the Continental Illinois situation in the early 1980s. In the mid-1970s the management of Continental Illinois decided upon a growth strategy that focused on commercial and industrial lending.[130] For the short term, this growth strategy seemed to work with Continental Illinois's share prices and return on equity going up.[131] But this was a risky plan as Continental Illinois's loan-to-asset ratio was very high.[132] This risk, as it turned out, did not pan out. As Continental Illinois's debtors began to default, its share prices began to decline and it became apparent that, in the name of growth, Continental made some bad loans.[133] Corporations and large financial institutions with deposits at Continental Illinois, the seventh largest bank in the nation at the time,[134] became nervous about the stability of the bank and so started to pull out their money. Regulators feared a bank run and that Continental Illinois's failure would cause systemic failure as many small banks had deposits at Continental Illinois and they could fail if Continental Illinois were allowed to fail. As a result of this concern, the regulatory authorities stepped in with loans and attempted to find a merger partner. When no partner was found, the regulators bought Continental's bad debt and the Federal Deposit Insurance Corporation (FDIC) fully protected all of Continental Illinois's depositors regardless of the limits on deposit insurance.[135]

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129. 15 U.S.C.A. § 1013(a) (West 2009); St. Paul Fire & Marine Ins. Co. v. Barry, 438 U.S. 531, 539 (1978) (citing SEC v. Nat'l Sec. Inc., 393 U.S. 453, 460 (1969)); *see also* Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205, 211 (1979) (citing *Nat'l Sec., Inc.*, 393 U.S. at 459-60).

130. 1 FED. DEPOSIT INS. CORP., HISTORY OF THE EIGHTIES – LESSONS FOR THE FUTURE, AN EXAMINATION OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S, at 236 (1997), *available at* http://www/fdic.gov/bank/historical/history/235_258.pdf.

131. *Id.*

132. *Id.* at 239.

133. *Id.* at 240-41.

134. William A. Lovett, *Moral Hazard, Bank Supervision and Risk-Based Capital Requirements*, 49 OHIO ST. L.J. 1365, 1366 (1989); Fed. Deposit Ins. Corp., *supra* note 140, at 236.

135. Cybil White, *Riegle-Neal's 10% Nationwide Deposit Cap: Arbitrary and*

C. *Systemic Risk Analysis*

Decades after the Continental Illinois crisis there are still no set rules or formulas for too big to fail; just a patchwork of laws for the benefit of regulatory agencies to invoke the doctrine when they believe there is risk of systemic failure.[136] Systemic failure is, in essence, the domino effect;[137] if the insolvent institution in question poses the risk of taking down other institutions if allowed to fail, and that scenario would have a significant negative impact on the domestic economy, the government will step in to prevent the failure of the insolvent institution.[138]

The bail-out, or public funds funneled into the insolvent too big to fail institution, is one method the government may utilize to prevent systemic failure. Another method is merger. Here, the government regulators find a relatively healthy institution to take over the insolvent one. When a large bank becomes insolvent in addition to the systemic failure problem, the potential cost to the FDIC insurance fund may be so high that the regulators feel compelled to force a merger or provide bail-out funding to keep the bank solvent until a permanent solution can be found.[139] In the current economic crisis, the government utilized the bail-out and forced merger to avoid systemic failure and introduced a third – systemic risk in bankruptcy reorganization.[140]

Unnecessary, 9 N.C. BANKING INST. 347, 354-56 (2005); Kenneth A. Guenther, *The Outlook for Specialized Institutions in the World of the Too Big to Fail*, 8 ANN. REV. BANKING L. 467, 470 (1989); *Inquiry into Continental Illinois Corp. and Continental Illinois National Bank: Hearings Before the H. Subcomm. on Financial Institutions Supervision, Regulation and Insurance of the H. Comm. on Banking, Finance and Urban Affairs*, 98th Cong. 172-78 (1984) (statement of C. Todd Conover); 1 FED. DEPOSIT INS. CORP., HISTORY OF THE EIGHTIES – LESSONS FOR THE FUTURE, AN EXAMINATION OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S 243-44 (1997), *available at* www.fdic.gov/bank/historical/history/235_258.pdf.

136. Yomarie Silva, *The "Too Big to Fail" Doctrine and the Credit Crisis*, 28 REV. BANKING & FIN. L. 115 (2008); *see, e.g.*, 12 U.S.C § 1823(b) (2009) & 12 U.S.C. § 343.

137. Steven L. Schwarcz, *Systemic Risk*, 97 GEO. L.J. 193, 198-200 (2008).

138. David Reiss, *The Federal Government's Implied Guarantee of Fannie Mae and Freddie Mac's Obligations: Uncle Sam Will Pick Up the Tab*, 42 GA. L. REV. 1019, 1050-51 (2008); Christopher T. Curtis, *The Status of Foreign Deposits Under the Federal Depositor-Preference Law*, 21 U. PA. J. INT'L ECON. L. 237, 247 (2000); Bert Ely, *Revisiting an Old Debate: Do Banks Receive a Federal Safety Net Subsidy?*, 18 NO. 21 BANKING POL'Y REP. 1, 14 (1999).

139. Helen A. Garten, *Banking on the Market: Relying on Depositors to Control Bank Risks*, 4 YALE J. ON REG. 129, 146 (1986).

140. *Corporate Bankruptcies in America: The Boom in Busts*, ECONOMIST, July 4, 2009, *available at* 2009 WLNR 12851000; Edward Pekarek & Michela Huth, *Bank Merger Reform Takes an Extended Philadelphia National Bank Holiday*, 13 FORDHAM J. CORP. & FIN. L. 595, 605 (2008).

D. *Will Systemic Risk Analysis Work in an Antitrust Context?*

A solution to the too big to fail problem is to consider the possibility that a firm that is too big to fail is too big to exist.[141] Conventional wisdom seems to believe that allowing firms that pose systemic risk to fail, bankrupting them out of existence, is not the proper solution given the potential dire economic repercussions.[142] Perhaps, but that does not mean that there is no choice but to allow them to exist. If systemic risk is considered in the antitrust analysis, particularly under Sherman § 2 and Clayton § 7, divestiture may be used to break-up firms that pose such a systemic risk and mergers involving firms that pose systemic risk would not be allowed to go forward.[143]

A proposal to include a systemic risk analysis in antitrust law seems to be rather controversial with some arguing that it cannot be done under current antitrust law.[144] Such a conclusion seems to be based, in part, on an assumption that, in order to have violated Sherman § 2 or Clayton § 7, a defendant must have a certain level of market share or the market must be highly concentrated. Neither statutory law nor case law limits antitrust analysis in such a fashion.[145] Indeed, the primary policy behind antitrust law in the United States is to promote free markets and eliminate anticompetitive practices.[146] A systemic risk analysis allows for the fulfillment of this policy.

E. *Systemic Risk Analysis and Sherman § 2*

Sherman § 2 provides, in pertinent part: "Every person who shall monopolize, or attempt to monopolize, . . . any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, . . ."[147]

The verb "monopolize," as used in Sherman § 2, means to improperly obtain a dominant position in the market so as to exclude actual or potential competition.[148] "Practice short of complete monopoly but which tends to create a monopoly and to deprive the public of the

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141. Simon Johnson, *The Quiet Coup*, ATLANTIC, May 2009, at 10.

142. Silva, *supra* note 136, at 122-23.

143. J. Thomas Rosch, Comm'r, U.S. Fed. Trade Comm'n, Address at the New York Bar Association Annual Dinner: Implications of the Financial Meltdown for the FTC (Jan. 29, 2009), *available at* http://www.ftc.gov/speeches/rosch/090129financialcrisisnybarspeech.pdf [hereinafter Rosch Statement].

144. *Id.* at 8-9.

145. *See* Brown Shoe Co. v. United States, 370 U.S. 294, 320-22 (1962).

146. *See* City of Columbia v. Omni Outdoor Adver., Inc., 499 U.S. 365, 388 (1991).

147. 15 U.S.C.A. § 2 (West 2004).

148. Cape Cod Food Prods. v. Nat'l Cranberry Ass'n, 119 F. Supp. 900, 906 (D. Mass. 1954).

advantages from free competition in interstate trade offends the policy of the Sherman Act."[149]

The Supreme Court has held that a person may have "monopolized" under Sherman § 2 if it is established that there is: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.[150] This Article focuses on the first prong of this test; monopoly power, as the second prong does not need to be determined using a systemic risk analysis.

"Monopoly power" [151] has been defined as "the power to control prices *or* exclude competition" and may be inferred from a predominant market share.[152] This power to control prices or exclude competition has often been called market power,[153] so one may have monopoly power if one has sufficient market share to infer market power. Market share is determined by ascertaining the percentage of control of a product (product market) within a specified geographic area (geographic market).[154]

Although case law allows the inference of monopoly power from market share evidence, market share is merely a surrogate for monopoly power because monopoly power is difficult to determine.[155] So if a person has a sufficient market share, it may be inferred that he has monopoly power giving him a dominant position in the market so as to have the power to control prices or exclude actual or potential competition in violation of Sherman § 2. But is there another way to prove monopoly power as defined by the Supreme Court? Case law is silent on an alternative approach, but does not preclude the possibility.

F. *Too Big to Fail and Monopoly Power*

As a matter of economic reality, when a firm creates a systemic risk it is deemed too big to fail and the government intervenes with public

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149. Ala. Sportservice, Inc. v. Nat'l Horsemen's Benevolent & Protective Ass'n, Inc., 767 F. Supp. 1573, 1582 (M.D. Fla. 1991).

150. United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966).

151. Monopoly power and market power are terms that appear to be used interchangeably by courts and commentators. *See* HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY, THE LAW OF COMPETITION AND ITS PRACTICE 272-73 (3d ed.) (2005).

152. *Grinnell Corp.*, 384 U.S. at 571; United States v. E. I. du Pont De Nemours & Co., 351 U.S. 377, 391 (1956); HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY, THE LAW OF COMPETITION AND ITS PRACTICE 79, 81 (3d ed.) (2005).

153. HOVENKAMP, *supra* note 151, at 272-75.

154. *Id.* at 83.

155. *Id.* at 80-81.

funding, merger approval, and expedited bankruptcy.[156] Conversely, any competitors not too big to fail are allowed to fail and are thus excluded from competition.[157] Further, a firm that is too big to fail has an improper competitive advantage that is likely to result in the control of prices and exclusion of competition in that it can take greater risks than other firms without suffering the consequences of poor judgment.[158] Such a situation does not promote efficiency, nor is it the type of "risk taking that produces innovation and economic growth."[159] If monopoly power is indeed required for a Sherman § 2 violation, it would be difficult to assert that a firm that is a systemic risk does not have monopoly power when it can have such a direct impact on prices and competition.

G. *Systemic Risk Analysis Allows for Price Control*

If we are to continue defining monopoly power as the power to control prices or exclude competition, the first thing we must ask is "Does a systemic risk analysis establish a tendency to be able to control prices?" An institution that is a systemic risk can control prices in some industries because consumers know that that institution will not fail, and hence will be around to service a product or, in the case of financial services, will be there to pay accounts. Let us look at two examples from the current economic crisis, General Motors and Bank of America.

In the General Motors case, the too big to fail argument rested, in part, on the argument that failure in terms of filing for bankruptcy was not an option because, even under Chapter 11 reorganization, consumers would not buy a GM car if they thought GM might not be there to honor warranties.[160] While GM did ultimately file for bankruptcy under Chapter 11 reorganization after receiving bail-out funds, it did so with the government's assistance to ease the process, the government's guarantee of warranties to ease consumer fears, and the

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156. Edward Pekarek & Michela Huth, *Bank Merger Reform Takes an Extended Philadelphia National Bank Holiday*, 13 FORDHAM J. CORP. & FIN. L. 595, 605, 694-95 (2008).

157. In a free market, private parties are allowed to compete without government intervention. Andrew Beckerman-Rodau, *Patent Law – Balancing Profit Maximization and Public Access to Technology*, 4 COLUM. SCI. & TECH. L. REV. 1, 11 (2002); Walter Adams & James W. Brock, *Antitrust, Ideology, and the Arabesques of Economic Theory*, 66 U. COLO. L. REV. 257, 282 (1995); David Cole, *First Amendment Antitrust: The End of Laissez-Faire in Campaign Finance*, 9 YALE L. & POL'Y REV. 236, 240 (1991).

158. Aaron Unterman, *Innovative Destruction – Structured Finance and Credit Market Reform in the Bubble Era*, 5 HASTINGS BUS. L.J. 53, 72 (2009).

159. *See* Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 407 (2004).

160. *America's Car Industry: And Then There Were Two*, ECONOMIST, Oct. 30, 2008, *available at* 2008 WLNR 20820175.

government's cash for clunkers program to help sales post-bankruptcy.[161] The other two domestic automobile manufactured in the United States, Ford and Chrysler, received similar governmental assistance while international competitors such as Honda and Toyota do not seem to be considered for bail-out monies, government guarantees of warranties, or bankruptcy preferences. How does this affect the ability to control price? With the government providing support, GM sales managed to improve despite all of its financial problems while Toyota and Honda sales declined.[162] Such government intervention off-sets the cost of doing business for GM thus allowing GM to sell its product at a lower price than its competitors without similar government subsidies. There is a plethora of evidence that government subsidies enhance a firm's ability to control price.[163]

As for the Bank of America example, once again we have the price controlling phenomenon of government subsidization of the too big to fail firm.[164] Specifically, a year after Bank of America received its government subsidy for being a systemic threat to the economy it raised its fees to its customers while smaller banks that were not subsidized by the government had to lower their fees in order to compete because customers would rather deal with a too big to fail bank than one the government would let fail.[165]

H. *A Too Big to Fail Firm May Eliminate its Competitors*

Certainly, a too big to fail firm has a competitive advantage in that it is, in essence, insured or subsidized by the government so it will not be allowed to fail. For example, in the financial services sector from January 1, 2009 to October, 2009, 89 FDIC financial services firms

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161. Warrantee Commitment Program, www.whitehouse.gov/assets/documents/warrantee_commitment_program.pdf (last visited Apr. 12, 2010); Car Allowance Rebate Program, Supplemental Appropriation Act, 2009, Pub. L. 111-32; Ken Bensinger & Jim Puzzangher, *"Cash for Clunkers" Gives a Boost to July Auto Sales*, CHI. TRIB., Aug. 4, 2009.

162. Andrew Ganz, *May Sales: GM, Ford Surprisingly Strong While Honda, Toyota Falter*, LEFT LANE, June 2, 2009, http://www.leftlanenews.com/may-2009-sales-figures.html (last visited Apr. 12, 2010); VOA News, *Major Automakers' US Car Sales Plunge in May*, VOA NEWS, June 2, 2009.

163. Frank A. Seminerio, *A Tale of Two Subsidies: How Federal Support Programs for Ethanol and Biodiesel can be Created in Order to Circumvent Fair Trade Challenges Under World Trade Organization Rulings*, 26 PENN ST. INT'L L. REV. 963, 973 (2008); Ved P. Nanda, *Selected Aspects of International Trade and the World Trade Organization's DOHA Round: Overview and Introduction*, 36 DENV. J. INT'L L. & POL'Y 255, 265 (2008); Andrew Green, *You Can't Pay Them Enough: Subsidies, Environmental Law, and Social Norms*, 30 HARV. ENVTL. L. REV. 407, 408 (2006).

164. David Cho, *Banks "Too Big to Fail" Have Grown Even Bigger*, WASH. POST, Aug. 28, 2009.

165. *Id.*

have been allowed to fail[166] while too big to fail financial institutions were bailed-out with public funds and allowed to buy failing institutions with public bail-out money further exacerbating the concentration level problem.[167] When the empirical evidence so clearly establishes an elimination of competitors that is not a natural consequence of efficiency, innovation, and free market forces but rather an unfair competitive advantage a market share analysis is not necessary.[168]

Accordingly, a firm that is too big to fail may violate Sherman § 2 because it has unacceptable monopoly power. Further, from a broader antitrust policy point of view, too big to fail firms skew the free market due government intervention. More could be done to promote a free market by utilizing antitrust law to eliminate systemic risk than by attempting to manage the risk through regulation.[169]

I. *Mergers Under Clayton § 7 and Too Big to Fail*

In enacting Clayton § 7 and its amendments, Congress was concerned with arresting concentration trends before they became a problem sufficient to constitute a violation of the Sherman Act.[170] "Thus, a merger may violate § 7 of the Clayton Act merely because it poses a serious threat to competition and even though the evidence falls short of proving the kind of actual restraint that violates the Sherman Act, ..."[171] Clayton § 7 provides, in pertinent part:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be *substantially* to lessen competition, or to tend to create a monopoly.[172]

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166. FDIC, Failed Bank List, http://www.fdic.gov/bank/individual/failed/banklist.html (last visited Apr. 12, 2010).

167. Cho, *supra* note 164.

168. *See* United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966).

169. Stephen G. Breyer, *Antitrust, Deregulation, and the Newly Liberated Marketplace*, 75 CAL. L. REV. 1005, 1006-07 (1987).

170. Brown Shoe Co. v. United States, 370 U.S. 294, 317 (1962); United States v. Von's Grocery Co., 384 U.S. 270 (1966) (Stewart J., dissenting).

171. Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 125 (1986).

172. 15 U.S.C. § 18 (1914) (emphasis added).

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"Congress used the words '*may be substantially to lessen competition,*' to indicate that its concern was with probabilities, not certainties."[173] It is a "prophylactic measure"[174] intended to prevent the anticompetitive effects in their incipiency.[175] While Congress did not specify any test to be used in determining whether a proposed merger may substantially lessen competition,[176] courts have recognized the relevance of economic data,[177] including market share,[178] and concentration levels.[179] However, statistics concerning market share and concentration levels are not conclusive indicators of anticompetitive effects.[180] Rather, a merger has to be viewed functionally, in the context of its particular industry[181] and take into account a particular market's structure and history.[182]

The method of determining market share has already been discussed above. Market concentration may be determined by a dramatic increase in the Herfindahl-Hirschman Index (HHI) as articulated in the U.S. Department of Justice, Merger Guidelines § 1.5 (1997).[183] However, the Merger Guidelines are not binding upon courts.[184] Further, "the Guidelines neither dictate nor exhaust the range of evidence that the Agency must or may introduce in litigation."[185]

173. *Brown Shoe*, 370 U.S. at 323.

174. Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 485 (1977).

175. FTC v. Procter & Gamble Co., 386 U.S. 568, 577 (1967); Rosch statement, *supra* note 143.

176. *Brown Shoe*, 370 U.S. at 321-22.

177. *Id.* at 322 n.38.

178. United States v. Phillipsburg Nat'l Bank & Trust Co., 399 U.S. 350 (1970); *Brown Shoe*, 370 U.S. at 321-22; United States. v. Gen. Dynamics Corp., 415 U.S. 486, 498 (1974).

179. *Phillipsburg Nat'l Bank*, 399 U.S. at 350; *Brown Shoe*, 370 U.S. at 321-22; *Gen. Dynamics*, 415 U.S. at 498.

180. William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases*, 94 HARV. L. REV. 937, 947-52 (1981).

181. *Brown Shoe*, 370 U.S. at 321-22; *Gen. Dynamics*, 415 U.S. at 498.

182. *Brown Shoe*, 370 U.S. at 322 n.38.

183. The Herfindahl-Hirschman Index measures of market concentration by squaring the market share of each firm competing in the market and then summing the resulting numbers. For example, for a market consisting of four firms with shares of thirty, thirty, twenty and twenty percent, the HHI is 2600 (302 + 302 + 202 + 202 = 2600). Markets in which the HHI is between 1000 and 1800 points are considered to be moderately concentrated and those in which the HHI is in excess of 1800 points are considered to be concentrated. Transactions that increase the HHI by more than 100 points in concentrated markets presumptively raise antitrust concerns under the Horizontal Merger Guidelines issued by the U.S. Department of Justice and the Federal Trade Commission. *See* U.S. Dep't of Justice and Fed. Trade Comm'n Horizontal Merger Guidelines § 1.51 (1992) (revised 1997).

184. Fed. Trade Comm'n v. Whole Foods Mkt., Inc., 548 F.3d 1028, 1046 (D.C. Cir. 2008).

185. U.S. Dep't of Justice and Fed. Trade Comm'n Horizontal Merger Guidelines § 0.1 (1992) (revised 1997).

https://scholarship.law.ufl.edu/fjil/vol22/iss1/2

The problem with merger analysis when it comes to the financial services sector is that there has been little Court guidance in this area since *Philadelphia Bank*[186] in 1963 and *Connecticut National Bank*[187] in 1974. Economic realities have greatly changed since the Court has expressed an opinion in these cases. From the 1970s through 2000 banking has changed from a "cluster of [banking] products"[188] in limited regions to one stop shopping financial services supermarkets that are nationwide and, in some cases, worldwide.[189] Despite this change in economic realities, regulatory agencies have continued to review mergers in the financial services sector, as if we still had "banks" with a simple cluster of banking products, conducting regional business as in the days of yore.[190] This has resulted in questionable economic data input for market share and concentration level analysis and the approval of many mergers, which has, in turn, increased concentration levels[191] and resulted in the creation of firms that are too big to fail.[192] Nothing in the statutory or case law requires a court to blind itself to these economic realities.[193]

J. *Systemic Risk Analysis*

It has been argued that the mere fact that a firm's failure is likely to cause a catastrophic effect on the market should be enough to find a substantial lessening of competition.[194] This holistic approach may negate the need to determine the relevant market due to the nature of the systemic failure causing cross-market reductions in competition. Thus, if there is systemic risk there is a probability of a violation of Clayton § 7. But the Supreme Court in *Brown* indicated that it was critical to determine the relevant market in order to determine if there is a probability of a substantial lessening of competition.[195] Accordingly, it

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186. United States v. Phila. Nat'l Bank, 374 U.S. 321 (1963).

187. United States v. Conn. Nat'l Bank, 418 U.S. 656 (1974).

188. *Id.* at 664.

189. Sharon E. Foster, *Fire Sale: The Situational Ethics of Antitrust Law in an Economic Crisis*, 78 MISS. L.J. 777, 784-87 (2009).

190. *See, e.g.*, Order Approving the Acquisition of a Savings Association and Other Nonbanking Activities (June 5, 2008); *see also* Order Approving the Acquisition of a Savings Association and an Industrial Loan Company (Nov. 26, 2008).

191. Wilmarth, *supra* note 20, at 250-54.

192. DAVID BALTO, RESTORING TRUST IN ANTITRUST ENFORCEMENT (Center for American Progress) (May 2009).

193. *Conn. Nat'l Bank*, 418 U.S. at 662.

194. Rosch Statement, *supra* note 143; Interview by Antitrust Newsmaker with J. Thomas Rosch, Comm'r, U.S. Fed. Trade Comm'n, (2009), *available at* http://www.ftc.gov/speeches/rosch/090126abainterview.pdf.

195. Brown Shoe Co. v. United States, 370 U.S. 294, 324 n.41 (1962).

may still be necessary to identify the product and geographic market.

Although the structure of the U.S. banking market has certainly changed since *Philadelphia Bank*,[196] the Court there broadly defined the product as "various kinds of credit" and services.[197] Economic reality would dictate that this would now include investment banking, commercial banking, and insurance. Because the assets held by a financial services institution is a measure of the credit and services it can extend, courts should consider, for product identification purposes, the assets held by a financial services firm in the relevant geographic market.[198]

As for the geographic market, the Court in *Philadelphia Bank* held that this is the area where the bank operates and the customer can reasonably turn for services.[199] Currently, the three largest financial services firms in the United States, J.P. Morgan, Bank of America, and CitiGroup, do business through-out the United States.[200] These three firms control approximately 44% of the financial services assets in the United States.[201] This is especially significant given the fact that concentration levels are growing.[202] Further, there is already some evidence that this size market share has substantially effected competition as the larger banks can, and have, raised prices (fees) to their customers with impunity.[203] Smaller banks cannot compete because they have to pay more to borrow money and do not have the "safety net" of too big to fail.[204] The concern of over concentration meant to be addressed by Clayton § 7 has been realized.[205] Finally, Clayton § 7 was intended to be prophylactic. As we can see, systematic

196. Wilmarth, *supra* note 20, at 250.

197. United States v. Phila. Nat'l Bank, 374 U.S. 321, 356-57 (1963).

198. *See* Order Approving the Acquisition of a Savings Association and an Industrial Loan Company (Nov. 26, 2008).

199. *Phila. Nat'l Bank*, 374 U.S. at 359.

200. Statistical Release, Fed. Reserve, Insured U.S. – Chartered Commercial Banks That Have Consolidated Assets of $300 Million or More, Ranked by Consolidated Assets as of June 30, 2009 (June 2009), *available at* http://www.federalreserve.gov/releases/lbr/current/default.htm.

201. *Id.*

202. Last year the same three banks controlled approximately 30% of financial service assets in the United States. Statistical Release, Fed. Reserve, Insured U.S. – Chartered Commercial Banks That Have Consolidated Assets of $300 Million or More, Ranked by Consolidated Assets as of June 30, 2008 (June 2008), *available at* http://www.federalreserve.gov/releases/lbr/2080630/default.htm.

203. U.S. GOV'T ACCOUNTABILITY OFFICE, BANK FEES: FEDERAL BANKING REGULATORS COULD BETTER ENSURE THAT CONSUMERS HAVE REQUIRED DISCLOSURE DOCUMENTS PRIOR TO OPENING CHECKING OR SAVINGS ACCOUNTS (2008), *available at* http://www.gao.gov/new.items/d08281.pdf; Cho, *supra* note 164.

204. Cho, *supra* note 164.

205. Wilmarth, *supra* note 20, at 250-54.

risk problems may cause an increase in concentration levels, a reduction in competition and an increase in prices. Accordingly, systemic risk analysis is a factor that should be considered in a merger review.

IV. THE ANTITRUST ANTIDOTE FOR TOO BIG TO FAIL IS UNLIKELY TO WORK IF THE END RESULT IS DOMESTIC FINANCIAL SERVICE FIRMS THAT ARE TOO SMALL TO COMPETE IN THE GLOBAL ECONOMY

There is no doubt that de facto and de jure deregulation of the financial services sector in the United States was based, in part, on a reaction to foreign competition concerns. The history of de facto deregulation establishes a parallelism of behavior with regulators in the United States allowing financial service firms to conduct more questionable business in order to compete with their under regulated European counterparts. For example, the 1989 CFTC Swap Policy Statement, effectively deregulating most swap transactions, came out the same year as the European Union's Second Banking Directive which deregulated European Union financial services firms. Then, there was the permission granted to J.P. Morgan in 1990 to conduct investment banking along with its commercial banking business which European Union commercial banks were allowed to do under the Second Banking Directive; or perhaps the example of de jure deregulation in the United States in 1994 with the passage of the Riegle-Neal Interstate Banking and Branching Efficiency Act allowing commercial banks to engage in interstate banking similar to commercial banks in the European Union being allowed to do cross border banking under the Second Banking Directive.

One may argue that such parallelism of behavior is insufficient circumstantial evidence to establish the connection between deregulation in the United States and the European Union. Perhaps, but then again there is more direct evidence. During the 1990s the congressional record is replete with comments regarding the urgency in passing financial services reform repealing Glass-Steagall so financial services firms in the United States could compete with foreign competitors.[206] Additionally, law review articles addressed the issue of foreign competition in financial services[207] and some called for

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206. *See, e.g.*, 144 CONG. REC. H3122 & H3124 (1998); 144 CONG. REC. H3133, H3135, H3137-38, H3140, H3142-43 (1998); 145 CONG. REC. S4737, S4742-43 (1999); 145 CONG. REC. H11515, H11519-23, H11525, H11527-28, H11533-34, H11536-38, H11543-45, H11547-48, H11550 (1999).

207. Wilmarth, *supra* note 20, at 234-35.

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deregulation in the name of international competition.[208]

Given the regulatory-deregulatory merry-go-round pattern that appears on a domestic and international scale, there is cause to be skeptical about a long term resolution to the financial crisis based, primarily, upon domestic re-regulation. What is needed is an elimination of systemic risk through divestiture and merger review but this must be done on an international level or it will not be done at all.

A. *International Competition and Too Big to Fail*

Let us assume, hypothetically, that antitrust law in the United States does address the too big to fail problem, and through divestiture and refusal to allow certain mergers to go through, reduces the too big to fail financial services firms to a manageable size. Domestic systemic risk is solved, but what about international competition and systemic risk?

The U.S. financial services sector has contributed significantly to the domestic economy over the years and its ability to do so in the future may be hampered by its inability to compete with foreign financial services firms that are too big to fail.[209] This is the very concern that contributed to the deregulatory cycle and ultimate financial meltdown. Given the domestic economic ramifications and the interconnectedness of the global economy[210] it is unlikely that the United States can go it alone — use antitrust law to break-up its financial services sector when other countries fail to do so.

The antitrust authorities and courts in the United States could use antitrust laws on foreign firms that are too big to fail in merger approvals under the doctrine of extraterritorial jurisdiction,[211] preventing financial services mergers that cause an effect in the United States, but this is a very contentious course of action.[212] If antitrust, as

208. Wagman, *supra* note 20, at 1005.

209. MICHAEL R. BLOOMBERG & CHARLES E. SCHUMER, SUSTAINING NEW YORK'S AND THE US' GLOBAL FINANCIAL SERVICES LEADERSHIP 34-36 (2007).

210. *See* Donald L. Kohn, Vice Chairman, Bd. of Governors of the U.S. Fed. Reserve Sys., Address at the 2008 International Research Forum on Monetary Policy: Global Economic Integration and Decoupling (June 26, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/kohn20080626a.htm; *see also* Randall S. Kroszner, Governor, Bd. of Governors of the U.S. Fed. Reserve Sys., Address at the Central Bank of Argentina 2008 Money and Banking Conference: The United States in the International Financial System: A Separate Reality? Resolving Two Puzzles in the International Accounts (Sept. 1, 2008), *available at* http://federalreserve.gov/newsevents/speech/kroszner20080901a.htm.

211. Laker Airways Ltd. v. Sabena, Belgian World Airlines, 731 F.2d 909, 940 (D.C. Cir. 1984); Gushi Bros. Co. v. Bank of Guam, 28 F.3d 1535, 1543-44 (9th Cir. 1994); Sharon E. Foster, *While America Slept: The Harmonization of Competition Laws Based Upon the European Union*, 15 EMORY INT'L L. REV. 467, 487-89 (2001).

212. Foster, *supra* note 211, at 485-86; Jeffrey M. Peterson, *Unrest in the European Commission: The Changing Landscape and Politics of International Mergers for United States*

an antidote is going to work, it must be done on an international scale.

B. *Harmonized Antitrust (Competition) Law*

Harmonized antitrust law would require an international agreement whereby the parties accept a uniform international antitrust law.[213] The concept of harmonized antitrust law takes us down a road well traveled but not well received.[214] During most of the 1990s the United States and European Union discussed the concept but had little agreement. The United States preferred a course of cooperation and coordination between competition authorities rather than harmonization.[215] The reason for the reluctance was based, in part, on the differing economic conditions of the various states and issues of sovereignty regarding domestic economic policy.[216] From 2000 to the present there has been little further discussion on the topic.

It is unlikely that the difficulties of the past relating to harmonized antitrust law could be overcome today; however, it is possible to have partial harmonization where there is an international agreement to integrate systemic risk analysis in domestic antitrust laws. There seems to be international consensus that systemic risk must be avoided.[217] The financial meltdown caused, in part, by systemic risk, harmed many domestic economies as well as the global economy.[218] It is evident that a free market cannot exist in an environment where a few firms can bring the global economy to its knees.[219] Accordingly, united action is necessary. As Benjamin Franklin once said, "We must all hang together, or assuredly we shall hang separately."[220]

Companies, 24 HOUS. J. INT'L L. 377, 405-06 (2002).

213. Foster, *supra* note 212, at 472.

214. *Id.* at 498-506.

215. *Id.* at 506, 509.

216. *Id.* at 498, 502, 505-06.

217. GROUP OF TWENTY, THE GLOBAL PLAN FOR RECOVERY AND REFORM (2009), http://www.g20.0rg/Documents/final-communique.pdf (last visited Apr. 12, 2010); Obama Remarks, *supra* note 125; Dominique Strauss-Kahn, Managing Dir., Int'l Monetary Fund, Speech at Oesterreichische National Bank: Crisis Management and Policy Coordination: Do We Need a New Global Framework? (May 15, 2009), *available at* http://www.imf.org/external/np/speeches/2009/051509.htm.

218. BANK FOR INT'L SETTLEMENTS, BIS QUARTERLY REVIEW: INTERNATIONAL BANKING AND FINANCIAL MARKET DEVELOPMENTS 1-12 (2008).

219. Albert A. Foer, *Preserving Competition After the Banking Meltdown*, GCP — THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY, Dec. 2008, at 2-5; Ben S. Bernanke, Chairman of the Board of Governors of the Federal Reserve System, Address at the 2008 International Monetary Conference: Remarks on the Economic Outlook (June 3, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20080603a.htm.

220. JOHN BARTLETT, FAMILIAR QUOTATIONS (William Hodge ed., 1980) (1937).

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V. CONCLUSION

The financial crisis of 2008-2009 has generated a considerable amount of discussion in both the popular press and academia. One obvious solution to this complex problem is to eliminate systemic risk through antitrust divestiture and merger review for systemic risks. Unfortunately, it would seem that most world leaders are content to enter, yet again, the regulatory cycle with promises of better regulation, especially for the too big to fail firms. Regulations may work but what happens when, somewhere down the road regulators don't regulate? What happens when there is a change in economic and political philosophy regarding regulations? Will we, yet again, deregulate? Are we doomed to a never ending regulatory cycle with similar booms and busts like the business cycle? Since we have identified a critical problem of systemic risk is it not advisable to eliminate that risk rather than hopefully reduce it through regulations?

In the United States, domestic antitrust law does provide a mechanism to eliminate systemic risk. Systemic risk analysis may be used to establish power to control prices or exclude competition for purposes of Sherman § 2 and may be used to show that a merger may substantially lessen competition as required under Clayton § 7. So, on a domestic front, antitrust law can eliminate the too big to fail problem but, as a practical matter, this will never happen so long as other states refuse to address systemic risk through antitrust laws. It was international competition that created a lack of regulatory oversight and financial service firms that are now too big to fail for fear that they would be too small to compete. Accordingly, unless there is an international response that too big to fail is too big to exist we shall continue down this road to Calvary.