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Financial choice act would improve stability

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After the bank bailouts of 2008, the public was promised "never again." Unfortunately the same congressional architects of that bailout, Sen. Chris Dodd and Rep. Barney Frank, enacted legislation giving regulators the permanent option of bailouts, as enshrined in the Dodd-Frank Act.

It is time for Congress to deliver on the "no bailout" promise. And Rep. Jeb Hensarling has a plan to do just that in his Financial Choice Act.

Core to the Choice Act is a move to improve financial stability by increasing bank capital, while reducing reliance on the same regulators who missed the last crisis.

While I would have chosen a different level of capital, the Choice Act gets at the fundamental flaw in our financial system: Government guarantees push banks to reduce capital that, unfortunately, leads to excessive leverage and widespread insolvencies whenever asset values (such as houses) decline.

Massive leverage still characterizes our banking system, despite the "reforms" in Dodd-Frank. Even ardent supporters of Dodd-Frank, such as economist Larry Summers, have recently concluded it has not made banks safer.

The Choice Act modestly improves oversight of the Federal Reserve. No contributor to the housing boom and bust has been as ignored by Congress as much as the Fed, and its reckless monetary policies in the mid-2000s.

Years of negative real rates drove a boom in our property markets. Stanford economist John Taylor has written extensively and persuasively on this topic, yet it remained ignored by Congress. Such reforms are too late to unwind the Fed's current distortionary policies, but they may moderate future booms and busts.

The fact is that Dodd-Frank has not made our financial system safer. Repealing all or large parts of it would, if anything, improve financial stability.

The Choice Act is best viewed as a modest step in the right direction. More needs to be done to bring market discipline and accountability to our financial system. But at least the Choice Act moves us in the right direction, for that the bill merits applause.

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