Binding Regulators

Mark Calabria says that instead of regulating big banks, we should just promise not to bail them out:

> *Since I believe most of us actually want to end "too big to fail," the real question is how to do it. It strikes me that we have three options: regulate the largest institutions to death (or competitive disadvantage), break them up, or credibly impose losses on their creditors. Ultimately I think the regulation approach is bound to fail, if for no other reason than regulatory capture. (Even Elizabeth Warren seems to get this: "Regulations, over time, fail. I want to see Congress focus more on a credible system for liquidating the banks that are considered too big to fail.") Breaking them up might sound attractive in theory, but I have a hard time seeing how it truly works in practice. After all, few in Washington viewed Bear Stearns as "too big to fail."* ***Accordingly, I believe the best approach would be to force creditors to take losses or be converted into equity. To make this credible, we must bind the hands of the regulators. As long as the Fed, Treasury, or the FDIC can inject money, then bailouts are always on the table****.*

I don't understand this on two levels. One is how do "bind the hands" of Treasury so as to prevent bailouts? It's *already* the case that Treasury can't conduct a bailout without congress appropriating the funds. That's why congress passed TARP. If there'd been a pre-existing law on the books saying "don't pass TARP" that wouldn't have stopped the 111th Congress from passing TARP any more than any of the members of the 111th Congress won their seats promising bank bailouts.

On the second level, this seems to me like a big-time incidence of the right's love of the regulatory capture hand wave. It's true that any effort at regulation are likely to be somewhat undermined by regulatory capture. But it's not like refusing to regulate banks *causes* banks to lose political influence. They'll exercise it to create pro-bank regulations, pro-bank tax policies, and (in the event of a crisis) banker-friendly bailouts. If you have large firms, they're going to seek to influence the political process. You can't wield this as a knock-down argument against regulation and then turn around and say that in lieu of trying to do effective regulation you're going to "bind the hands" of public officials. It's not like the government is going to just not have a Treasury Department or that congress will lose its authority to appropriate money.