If Elizabeth Warren wants to lay blame for financial mess, she can look in the mirror

By Erick Erickson February 18, 2013

Chairman of the U.S. Federal Reserve Ben Bernanke attends the summit of financial ministers and heads of central banks of the G20 group of nations ahead of their meeting in Moscow, Russia, Saturday, Feb. 16, 2013. (AP Photo/Misha Japaridze) (AP2013)

A video has been making the rounds of Sen. Elizabeth Warren, D-Mass., getting non-answers from various regulators during her first Banking, Housing and Urban Affairs Committee hearing.

Warren asked a very simple question to the various regulators — “Can you identify the last time when you took the Wall Street banks to trial?” The FDIC, SEC, Federal Reserve, Treasury Department and other regulators have not taken any Wall Street banks to trial.

The closest the federal government will go to taking anyone to trial over the financial crisis and housing meltdown will be a lawsuit against Standard & Poor’s Ratings Services for, in the words of the Department of Justice press release,

a scheme to defraud investors in structured financial products known as Residential Mortgage-Backed Securities (RMBS) and Collateralized Debt Obligations (CDOs). The lawsuit alleges that investors, many of them federally insured financial institutions, lost billions of dollars on CDOs for which S&P issued inflated ratings that misrepresented the securities’ true credit risks. The complaint also alleges that S&P falsely represented that its ratings were objective, independent, and uninfluenced by S&P’s relationships with investment banks when, in actuality, S&P’s desire for increased revenue and market share led it to favor the interests of these banks over investors.

There are surely those who should be sued or prosecuted for the financial crisis, but the best anyone could actually do is vote the bulk of the culprits out of office.

The banks themselves have been left alone. Regardless of political persuasion, many have wondered why no banks were prosecuted or otherwise sued in civil litigation for the financial crisis and housing market meltdown. What most miss is that many of the banks were only doing what the federal government made them do.

Former Treasury Secretary Hank Paulson forced many banking institutions into accepting TARP funds during the financial crisis, threatening the well-run banks with increased regulator action.

Paulson and Federal Reserve Chairman Ben Bernanke sent Bank of America into a tailspin, forcing it to buy Merrill Lynch even though Bank of America wanted out of the deal. According to the Wall Street Journal, Bank of America CEO Ken Lewis

told investigators for New York Attorney General Andrew Cuomo that in December Mr. Paulson threatened him not to cancel a deal to buy Merrill Lynch. BofA had discovered billions of dollars in undisclosed Merrill losses, and Mr. Lewis was considering invoking his rights under a material adverse condition clause to kill the merger. But Washington decided that America's financial system couldn't withstand a Merrill failure, and that BofA had to risk its own solvency to save it.

The Treasury Department went on to approve big pay raises for AIG, Ally Financial and even General Motors, despite all their financial problems.

As the libertarian CATO Institute and others have noted, the federal government created the conditions, laws and regulations that directly led to the financial crisis. The Community Reinvestment Act, assorted regulations, Fannie Mae, Freddie Mac and Congress itself all created incentives and demands for banks to make bad loans to people who could not repay them. These laws, regulations and institutions all made it harder and harder for banks to make money in traditional ways, causing banks to take more and more risks to break even.

There are surely those who should be sued or prosecuted for the financial crisis, but the best anyone could actually do is vote the bulk of the culprits out of office. The rich irony of Elizabeth Warren asking her question to these regulators, whose ranks she would have joined but for a Republican effort to block her nomination prior to her Senate run, is that she is an advocate of increasing the very regulations that contributed to the financial meltdown and that prevent suits against Wall Street banks. After all, Wall Street was just complying with Washington’s orders.

In a final irony, the legislation designed to prevent this all from happening again, commonly called Dodd-Frank, has institutionalized the idea that certain banks are “too big to fail” and put smaller banks at a competitive disadvantage. More and more American assets are held by fewer and fewer banks thanks to ideas advocated by people like Sen. Elizabeth Warren.

If she wants a scalp, she should look in the mirror.