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## Lew-for-Geithner Switch Ends Era of Tight Fed-Treasury Ties

By: Rich Miller, Jeff Kearns & Ian Katz – January 10<sup>th</sup>, 2013

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**T**imothy F. Geithner's replacement by Jack Lew as Treasury secretary will end a period of unusually strong ties between the department and the Federal Reserve. For the Fed, the result may be less insulation from critics, yet greater influence in financial market regulation.

Geithner worked closely with Fed Chairman Ben S. Bernanke in fighting the financial crisis and cleaning up its aftermath, first as head of the Federal Reserve Bank of New York and then as Treasury secretary. Going through the "searing experience of the panic together" created a bond between the two that "you get from that kind of combat," Geithner said in a 2010 interview.

"You've never had a secretary with the type of credentials" that Geithner had, including his relationships and knowledge as a former Fed insider, said Edwin M. Truman, who has worked at both the central bank and under Geithner at the Treasury. "The only thing that comes close" was when Paul Volcker headed the Fed after being a senior Treasury official.

President Barack Obama will announce at 1:30 p.m. in Washington that he plans to name Lew, his White House chief of staff, to replace Geithner at the Treasury, according to a person familiar with the process.

Geithner's departure means the central bank will lose a strong ally inside the executive branch who helped protect the Fed from efforts by both Republican and Democratic lawmakers to rein in its power.

### ***Little Sympathy***

While Lew would have no more sympathy than Geithner for assaults on the Fed, "I don't expect him to be as defensive of the Fed and as quick to attack those things as Geithner would be," said Mark Calabria, a former aide at the Senate Banking Committee to Alabama Republican Richard Shelby. Calabria is now director of financial regulation studies at the Cato Institute in Washington.

Lew, 57, also lacks the experience that the 51-year-old Geithner had with international financial markets and regulation, leaving an opening for others inside the government, including at the Fed, to gain more sway in that area.

Fed Governor Daniel Tarullo may be one who does that, especially in meetings of the Financial Stability Oversight Council, which brings together regulators across the government and is headed by the Treasury secretary.

“With Geithner’s departure, Tarullo is now one of the more dominant personalities in the room at FSOC meetings, allowing him to leave a larger imprint on regulations,” said Brandon Barford, another former Shelby aide who is now a vice president at ACG Analytics Inc., a Washington research and consulting firm.

### ***Shifting Priorities***

The anticipated nomination of Lew to head the Treasury highlights a shift in the economic priorities of the Obama administration, away from battling the crisis and overhauling financial regulation to working with Congress to tackle a budget deficit that’s topped \$1 trillion for four straight years.

Lew’s skill set may be better suited to the times. While it was important for Geithner to have experience dealing with economic emergencies when he took over Treasury in 2009, now “the number-one challenge is different,” said Martin Baily, who worked with both Lew and Geithner under former President Bill Clinton.

“Jack will bring to the budget challenge a lot of experience,” said Baily, now a senior fellow at the Brookings Institution in Washington, who was chairman of Clinton’s Council of Economic Advisers.

### ***Budget Director***

Before becoming chief of staff, Lew served as Obama’s director of the Office of Management and Budget, a position he also held in the Clinton administration. Lew’s anticipated nomination is subject to Senate confirmation.

Geithner’s experience in fighting financial fires, both as a Treasury official in the Clinton administration, when he was involved in dealing with Asia’s economic woes, and later as president of the New York Fed, allowed him to hit the ground running when he became secretary in 2009, Truman said.

He also benefited from being well known internationally, including having a close relationship with European Central Bank President Mario Draghi, added Truman, a senior fellow at the Washington-based Peterson Institute for International Economics.

Geithner was unique as a Treasury secretary “because he was both a staffer at Treasury and an official in the Federal Reserve System before becoming secretary so he saw it from both levels, as career staff and leadership of the Fed,” said Tony Fratto, who worked at Treasury during the George W. Bush administration.

Geithner and Bernanke looked out for each other as they struggled to contain the worst financial crisis since the Great Depression and speed up the subsequent recovery of the economy.

### ***Geithner Ally***

In February 2009, Bernanke took Geithner’s side when the Treasury secretary was fighting calls for the government to take over large, ailing banks -- a step that Bernanke’s predecessor, Alan Greenspan, suggested might be necessary.

Geithner's alternative, dreamed up on a beach in Mexico while he was between his New York Fed and Treasury jobs, was to put the biggest banks through Fed stress tests before forcing them to take on more capital.

Later that year, Obama, advised by Geithner, nominated Bernanke to his second four-year term as Fed chairman.

The Geithner-Bernanke alliance was further cemented during the year-long debate over financial reforms, which Obama signed into law in July 2010. Led by Geithner, the administration fought off congressional efforts on Capitol Hill to rein in the central bank's independence.

### ***Audit-the-Fed***

"He helped defend the Fed against some of the excesses that were thrown around on the Hill like the audit-the-Fed movement," said Fratto, a partner at Hamilton Place Strategies, a policy and communications consulting firm in Washington.

The 59-year-old Bernanke said in 2010 that he and Geithner had "a lot of mutual trust."

The Fed chairman doesn't have anything like that close a relationship with Lew. His daybook shows that he hasn't had a meeting at his office with Lew since at least November 2010, when the budget maven took over OMB.

Lew, though, should be able to build a strong rapport with Bernanke because the interests of the two institutions are intertwined, Fratto said.

The next Treasury chief also may have a new opposite number at the Fed before too long. Bernanke's second term as chairman ends in January 2014 and the chances his staying on "are quite low," according to former Fed Vice Chairman Donald Kohn, a 40-year veteran of the central bank. As he did with Geithner, Obama may consult Lew about who should be Fed chairman.

### ***Dodd-Frank***

Geithner is leaving Treasury at a time when some of the rule-making set out in the 2010 Dodd-Frank financial overhaul legislation has yet to be completed. Regulators still are working on writing provisions, including a proprietary-trading ban advocated by Volcker that's intended to reduce the chance banks will risk depositors' money.

The Fed's Tarullo also is pushing an agenda to regulate banks beyond the restraints in the law, including making them fund more of their assets using long-term borrowing.

Lew himself has said that regulation isn't his strongest suit. In an appearance before the Senate Budget Committee in 2010, he was asked by Senator Bernie Sanders, a Vermont independent, whether deregulation of Wall Street contributed to the economic crisis.

Lew said he didn't believe it was the "proximate cause," then added, "I would defer to others who are more expert about the industry to try and parse it better than that."