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Massachusetts Upset Could Mean Curtains for Obama's Tax

By Stacy Kaper, American Banker

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Among the many losers in Massachusetts' special election this week: the Obama administration's bank tax.

Democrats lost the Senate seat held by the late Sen. Edward Kennedy for 46 years as a Republican state lawmaker came from way behind to handily win Tuesday's election.

President Obama himself injected the tax issue into the special election, going to Massachusetts over the weekend to campaign for the Democratic candidate, Martha Coakley. The state's attorney general backed the fee as a payback for the financial bailout, but Scott Brown, whose victory cost the Democrats their filibuster-proof 60-seat majority in the Senate, opposed the tax, saying it would drive up consumer costs.

Sen. Judd Gregg, R-N.H., who sits on the Senate Banking Committee, said the administration should take a cue from Massachusetts voters.

"They ran a lot of ads on this issue, and Sen. Brown was equally clear that he felt that taxes at this time on this economy are counterproductive to job creation and economic growth," Gregg said in an interview Wednesday. "People sided with Sen. Brown for a lot of reasons, but obviously this could be regarded as one of them."

Daniel Forte, the president of the Massachusetts Bankers Association, agreed.

"What Scott tapped into was the cost of the rising deficit, and he struck the nerve of consumers," Forte said. "He's a very likable guy and a real hard worker, and I think that came across in the campaign."

Brian Gardner, an analyst with KBW Inc.'s Keefe, Bruyette & Woods Inc., predicted the bank tax would fade "pretty quickly."

Gardner noted that the administration and the Coakley campaign tried to frame Brown's opposition as siding with fat cats on Wall Street. "It didn't seem in the final days of the campaign that that argument got any traction whatsoever," he said. "I think Republicans have to be emboldened by that, and I think a number of Democrats who were leery of supporting another tax — even if some would try to explain it away as only on big institutions — I don't think there is as much support for that as the administration thought there would be."

Obama proposed the tax last week and will release more details on it Feb. 1 along with his fiscal 2011 budget proposal. It would levy a 15-basis-point fee against financial companies with more than $50 billion of assets. It would be assessed against net liabilities, or assets minus Tier 1 capital and domestic deposits. The administration has said it expects that 20 to 27 U.S. commercial banks would pay the fee, starting June 30. Investment banks and insurers would also be taxed as would the U.S. units of some foreign banks. The 10 largest companies are expected to pay 60% of the total $90 billion that the fee is to generate over the next 10 years.

Jaret Seiberg, an analyst with Washington Research Group, a division of Concept Capital, took a contrarian view and argued that the administration has not had time to build support for the bank tax. He suspects the loss in Massachusetts will cause Democrats to pivot harder to the left.

"You are really going to see the Democrats go on the attack and that means they are going to push a vote on the bank tax, bringing up pro-consumer issues like overdraft fee legislation and that even could give an added push for mortgage bankruptcy reform and consumer bankruptcy reform," Seiberg said.

While opinion may be mixed on the fate of the bank tax, observers overwhelmingly agreed that the Democrats' loss in Massachusetts would have little impact on regulatory reform legislation.

That's largely because it was already widely believed that to get enacted financial reform would need bipartisan support driven by Senate Banking Committee Chairman Chris Dodd of Connecticut and the ranking Republican, Richard Shelby of Alabama.

"There's not a big impact one way or another for reg reform," Gregg said. Most issues are "technical, difficult questions about how to get this right. ... They are not really philosophical, ideological differences."

Dodd, who recently announced he will retire at yearend, echoed that point Wednesday.

"I commend my Democratic colleagues on the committee, but also a number of Republicans on the committee, who before all of the events of last evening made a commitment to work on a bill together, despite, I think, the urgings of others to do just the opposite," Dodd told reporters. "We're really trying to get a consensus bill. We're going to try and make this work."

Asked if the Consumer Financial Protection Agency is dead, Dodd said "no," but also made it sound like the legislation was still in its preliminary stages. "Nothing has been agreed to at all, except a lot of conversation about various aspects of a very complicated set of issues. The idea that something has already been decided about any aspect of this bill is completely false."

Mark Calabria, the director of financial regulation studies at the Cato Institute and a former aide to Shelby, said the Massachusetts Senate election empowers Shelby.

"It's going to force Dodd to have to recognize the reality that was already there. He can no longer pretend that passing the bill on a party-line vote is an option," Calabria said. "The CFPA and permanent bailouts will have to be jettisoned."

Rep. Patrick McHenry, R-N.C., who serves on the House Financial Services Committee, took that analysis a step further.

"Shelby has the capacity to fix nine-tenths of the bill's problems," he said. "They need to get his support to get something through and Shelby has the capacity to kill it or fix it."

McHenry, who like most House Republicans also opposes the bank tax and the consumer agency, predicted the results in Massachusetts will cost the White House support among Democratic lawmakers.

"I think Democrats will largely embrace less of Obama's agenda now. He is going to be a lighting rod for this next election," McHenry said. "The more extreme elements like the bank tax and the CFPA after the Massachusetts Senate outcome are highly unlikely.

"The president needs a success, especially if health care implodes. ... I think at the end of the day they'll take what they can get [on regulatory reform] and call it a victory."

How Brown approaches these debates is unclear, but Forte of the Massachusetts Bankers, made a prediction based on a predatory lending bill Brown worked on.

"He's going to look at any type of regulatory bill two ways: how does it impact consumers and is there a way to implement change without hurting the competitiveness of the industry?" Forte said. "He did support the bill, which had heightened regulatory scrutiny of high-cost loans that applied to both banks and nonbanks, but it was something that we could live with and that provided protections to consumers."