

## [No wonder we have bank bailouts: regulators will always be captured by the firms they're meant to oversee](#) [1]

Written by [Sam Bowman](#) [2] | Tuesday 1 May 2012



One important free market argument against government regulation of the economy is that regulators tend to become captured by corporate interests. When faced with a brief they know little about, politicians turn to the experts to devise policy and advise them on the ins-and-outs of the different industries they're expected to regulate.

Who are those experts? Business leaders who've made their money by mastering their industry. The very people who stand to gain the most from some insider political power to protect themselves from competition. Firms are constantly looking for a way to exclude new entrants from the marketplace ? when governments have a lot of power over the market, the incentive for firms to try to bend that power to their will is overwhelming.

This is an unavoidable aspect of the fact that government officials ? politicians, civil servants, and even ?independent experts? the government loves to put in charge of its policy commissions ? are human. They are no more or less greedy or easily swayed than anybody else.

This concept of ?regulatory capture? is one reason I tend to prefer rules to individual discretion when thinking about regulation. There?s no way to ensure that only the angels get into power, and I'd prefer to avoid much discretionary power being invested in the hands of individuals, in case they misuse it.

All of this is important in understanding where we are and where we're going. One of the most remarkable phenomena of recent years has been the [revolving-door relationship between Goldman Sachs and the US government](#) [3]. Goldman Sachs is not a morally bad company, but its success has led to its executives being tapped up for senior roles in the Clinton, Bush and Obama administrations ? notably Hank Paulson, a former Goldman CEO who presided over the Troubled Asset Relief Program (TARP), the first major bailout for US banks during the financial crisis.

There is no need for conspiracy theories here. It is sufficient to presume that Paulson?s ties to the financial world made him sympathetic to calls for bailouts and to the idea that established firms in the financial sector could not be allowed to go bust in an orderly fashion.

Paulson is not, personally, the one to blame: the system that gave anybody the power to pervert the market with bailouts is. If Paulson had not been in that position, someone else had ? and if not someone tied up with Goldman Sachs, then with JP Morgan, CitiBank, or one of the other large banks. The mindset that these established firms have to be protected at any cost would be there, wherever the Treasury Secretary had come from.

All this came to mind yesterday when reading that [Goldman Sachs? Jim O?Neill is rumoured to be in the running](#) [4] to succeed Mervyn King as Director of the Bank of England. No doubt O?Neill has a lot of valuable experience ? although I find his much-celebrated categorization of the ?BRICs? (Brazil, Russia, India and China) as must-invest powerhouses slightly underwhelming. But, like all ex-financiers who enter the political-regulatory nexus, he would be beholden to the established firms that made him who he is today.

For different reasons, an academic may be little better, [unless he was a truly radical visionary](#) [5]. But, if O?Neill or someone like him gets the job, I know what response my money will be on when the next financial crisis rolls around.

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