Todd Zywicki (00:00:00):

And it's the classic male fist behind the velvet glove, right? Which is, Judge Willett says during the oral argument, "Nice little social media company here. It'd be too bad if something happened to it." Because the antitrust enforcers got interested.

Bill Walton (00:00:15):

They compared them to the mob.

Todd Zywicki (00:00:17):

Yeah. Right. Yeah. Right, right. Yeah. It's exactly what it is, right?

Bill Walton (00:00:22):

It's the mob.

Todd Zywicki (00:00:23):

It's the mob.

Bill Walton (00:00:23):

They don't have to say it to you.

Todd Zywicki (00:00:24):

Yeah, right. They don't have to say it. They don't even have to follow through, right? You just have to know that they might follow through, right? And that's what they can do with these things.

Bill Walton (00:00:36):

Well, here's my favorite new quote. Have you heard about Uncle Earl Long? He's the brother of Huey Long.

Todd Zywicki (00:00:47):

Yeah, right, in Louisiana.

Bill Walton (00:00:48):

He once said, "Don't write anything you can phone. Don't phone anything you can talk."

Todd Zywicki (00:00:54):

Right.

Bill Walton (00:00:54):

"Don't talk anything when you can whisper. Don't whisper anything when you can smile. Don't smile anything you can nod. And don't nod anything you can wink."

Todd Zywicki (00:01:06):

Right, right.

Speaker 3 (00:01:07):

The Bill Walton Show, August 16th.

Speaker 4 (00:01:13):

Welcome to the Bill Walton Show featuring conversations with leaders, entrepreneurs, artists and thinkers. Fresh perspectives on money, culture, politics and human flourishing. Interesting people, interesting things.

Bill Walton (00:01:34):

Welcome to the Bill Walton Show. I'm Bill Walton. We often talk about the need for the rule of law, but not very often do we really get into why it really matters, and adherence to the rule of law is essential for economic growth and especially personal liberty.

(00:01:53):

The rule of law consistently and fairly applied affords a clear legal landscape so that we can make plans and have confidence that we can carry them out. The rule of law enables us to anticipate other people's behavior, especially government officials, so that we can pursue our individual ends, whatever they may be.

(00:02:15):

Yet the rule of law is in steep decline in the United States, and perhaps no more so than in a field I spent most of my career in, the rule of law and finance and banking. This sounds like a boring topic, but it is not. Financial regulation is unusually convoluted and secretive and it affects you every single day.

(00:02:40):

And in particular, and we'll be talking about here this year, is that the clash between the rule of law and the coercive regulatory state affects every one of us, but most of us are not even aware it's occurring.

(00:02:53):

So with great fanfare, I'd like to bring in my guest, Todd Zywicki, returning guest, great friend, great friend of liberty especially, professor at George Mason's Scalia rule of law, who's written a terrific piece called Restoring the Rule of Law in Finance.

(00:03:11):

Todd's been back here many times. Last time he was here with Janine Unis, we were talking about Missouri v Biden, what it looks like so far, it looks like we might get it through appeals and have a win. And Todd's also talked to us about bringing, what do we call that? Chinese style social credit. We'll be coming to America, and we're also going to get into Central Bank digital currencies today, and how alarming they are and what we need to do about it. So Todd, welcome.

Todd Zywicki (00:03:43):

Thanks Bill.

Bill Walton (00:03:44):

And you've got a new gig. You're going out to Boulder.

Todd Zywicki (00:03:49):

That's right. I'm going to be the visiting scholar and conservative thought and policy for the Bruce Benson Center for the study of Western Civilization at the University of Colorado, Boulder for this fall.

Bill Walton (00:04:02):

So Boulder, that would make you their diversity hire for the year.

Todd Zywicki (00:04:05):

I think that would, that's right. That's right. My Birkenstocks are in the mail from Amazon.

Bill Walton (00:04:12):

And you're going to be teaching about the rule of law.

Todd Zywicki (00:04:14):

I'll be teaching two classes. One on the rule of law, the history, the theory, and the implications. And then I'm going to be teaching a class on Hayek and his critics, which, given Hayek's centrality of the rule of law, debate in the last century in particular, obviously these topics will be front and center in that class also.

Bill Walton (00:04:31):

So let's get into the rule of law in finance. I mean, we're going to wander into, I think, a lot of different things, but can you give us just the gist of why we ought to be concerned?

Todd Zywicki (00:04:42):

Sure. The rule of law in finance is important for two reasons, as you suggested in your introduction, which is first, it's the cornerstone of economic liberty. Ayn Rand once said, "You could think of money as a form of frozen energy."

(00:04:58):

Which is, it's sitting there to be unleashed for creative powers and economic growth. But to be able to make loans, to be able to get capital in the economy, you need to be able to rely on contracts. You need to be able to rely on the fact that contracts will be enforced, that the government won't act arbitrarily to take your property or rewrite contracts, because finance requires investments over long periods of time, 10, 20, 30 year bonds, even, things like that.

(00:05:29):

And so to the extent that finance, access to capital, access to banking services, is essential for economic freedom and economic growth, the rule of law, perhaps more than any other industry, is the center of that. But the second thing is, is the rule of law-

Bill Walton (00:05:46):

Well, otherwise, it's like playing any kind of board game with no rules.

Todd Zywicki (00:05:49):

Yeah, that's right.

Bill Walton (00:05:50):

And you can't get from here to there unless you know what the parameters are. And a businessman, and I've been in this mode deploying capital. If you don't know what's going to be the law five years from now, you can't deploy capital now.

Todd Zywicki (00:06:04):

That's exactly right.

Bill Walton (00:06:05):

And you look at economic growth in the countries throughout the world, those that have a firmer rule of law have much faster economic growth than those that don't.

Todd Zywicki (00:06:14):

Yeah, exactly right. Because you need it in order to be able to make investments. A good example is, if you recall back to the financial crisis of 2008 when the government bailed out the auto companies, and in particular in Chrysler, if you recall, the government came in, and for the benefit of the UAW, plundered the preexisting secure creditors in that case, and forced them to take less than they were entitled to.

(00:06:41):

What's interesting about that, that illustrates the point, Bill, is that after that, economic studies found that debt contracts changed, that if you were going to lend to a company and industry, particularly one that was heavily unionized, you demanded a risk premium that you did not previously demand, precisely because of the new political risk associated with the fact that the government might take an interest in the investment and intervene to help out some politically favored constituencies.

Bill Walton (00:07:12):

Well, let me put this in plain English, as a former deal guy. Basically, you make a loan to Chrysler and you say to Chrysler, "I'll give you the money, but I want a security interest in your assets, and that gives me collateral for my loan." So even though it's a risky credit, I'm okay because I know I've got enough assets to cover it if I've got to liquidate.

Todd Zywicki (00:07:33):

Right.

Bill Walton (00:07:33):

So what the government did here, at the behest of the labor unions, is they said, "Secured creditors, sorry, you don't have that security interest. You're just floating out the unsecured. And moreover, you're not only going to not get your money back, or not get your collateral, you're not going to get most of your money back."

Todd Zywicki (00:07:52):

Right.

Bill Walton (00:07:53):

That's what the government did.

Todd Zywicki (00:07:54):

That's right. And that has an impact, which is, studies found that going forward-

Bill Walton (00:07:59):

All of a sudden you're wondering why you want to put money into any automobile company.

Todd Zywicki (00:08:02):

Yeah, Wall Street may be greedy, but they're not stupid, right? After that, basically you're going to charge higher interest rates before you lend to those industries and the like. And that illustrates the importance of firm contractual obligations, firm reliable regulatory environment and the like.

(00:08:22):

But the rule of law in finance is important for a second reason, which is it's important for individual liberty. And one of the examples I give in this, that we'll come back to, is this new problem of de-banking, well, emerging problem of the past few years that I've been sounding the alarm about, and we've talked about previously, which is this idea of banks taking away people or organizations' financial, their bank accounts, for political reasons.

(00:08:54):

And this really started during the Obama administration under the Operation Choke Point Initiative, where they targeted completely legal industries such as firearms dealers, payday lenders, so-called sellers of so-called racist materials, and basically went to the banks and said, "It's a reputation risk to deal with companies in these industries." And so they lost access to bank accounts. Now this has happened-

Bill Walton (00:09:22):

The industries were pawn shops, gun dealers-

Todd Zywicki (00:09:25):

Gun dealers, they also-

Bill Walton (00:09:26):

Payday lenders-

Todd Zywicki (00:09:27):

Payday lenders. They also said things like "racist materials" and the like, notably, they did not include, say, abortion clinics, environmental groups and the like. So it's clearly a political list. But what I think is so striking about that, that goes beyond just the financial issue, is essentially what they were doing... You couldn't pass a law that prohibited gun dealers or racist companies or racist people, because the First and Second Amendment would prevent it.

(00:10:02):

But what we're seeing now is they can use this leverage of the financial system to stifle dissent, to essentially, in that example, take away First and Second Amendment rights. Because if you can't have a bank account, you can't really have a company that sells stuff to the public. And so it provides a way of, they called it Operation Choke Point for a reason, which is, they said the financial system is the choke point.

Bill Walton (00:10:28):

Very rarely do they name something so accurately.

Todd Zywicki (00:10:31):

That's right. That's right. But that shows the way in which individual liberty is threatened, our constitutional rights are indirectly threatened.

Bill Walton (00:10:40):

They just did this with Mike Lindell.

Todd Zywicki (00:10:42):

Exactly.

Bill Walton (00:10:43):

And they did it with... Who's the governor of Kansas that they ran?

Todd Zywicki (00:10:48):

Sam Brownback had a religious liberties organization that I believe it was Chase-

Bill Walton (00:10:56):

It was Chase,

Todd Zywicki (00:10:57):

It was Chase, said-

Bill Walton (00:10:58):

My good buddy, Jamie Diamond-

Todd Zywicki (00:10:59):

We want to know what you're doing. We want to know who your donors are going to be. We want to know who you're going to donate to, all these sorts of things, before we will give you a bank account. And so this shows the threat here right now. Do we know for sure that the administrative state and the government is behind it? No, but that gets to the question of how exactly the government is exercising its power in these areas.

Bill Walton (00:11:24):

We were talking about this before we got started here, was that, you and I go back long way as Libertarians, and the paradigm really was, okay, they're the private actors, the hardy entrepreneurs, the John Galts of the world, and they're off making, creating wealth. And then you've got the predatory government, and they're trying to shut companies down, take them over, make them do socially good things at their behest.

(00:11:51):

Well, now we're seeing a very different landscape. The big banks in particular, and a lot of the big multinational companies, their political agenda has become aligned with a lot of the government, a lot of the federal agencies. So we used to think just in terms of regulators. Now at Chase, you don't know whether there's some person in their department of community affairs who was a progressive, said, "We ought to shut Brownback back down."

Todd Zywicki (00:12:19):

And that's what I think is the important question for those of us who are libertarians and conservatives to confront, which we've had this-

Bill Walton (00:12:26):

By the way, I think everybody should be a Libertarian.

Todd Zywicki (00:12:28):

And everybody should, right. But we've had this kind of very useful binary view of the world for centuries, really, which is the private sector is not only neutral toward liberty, but private sector competitive markets is promotion of liberty. And so allowing private sector companies to decide who to deal with-

Bill Walton (00:12:50):

Promotional liberty, what do you mean?

Todd Zywicki (00:12:52):

That it actually furthers liberty to basically allow companies to be able to do this, where the public sector then is the only real threat to liberty. But what you put your finger on, and what I've been sort of sounding the bell on for the last several years is, in the world of the modern administrative state, that binary is no longer valued, is no longer completely accurate. So you gave the example of Chase, but you think about Chase or Citibank or Bank of America, I don't know what you call those, but to call those just a private company-

Bill Walton (00:13:28):

Especially after Dodd-Frank.

Todd Zywicki (00:13:29):

Yeah, especially after Dodd-Frank, like Sal's butcher shop on the corner, or Sally's beauty supply on Main Street, whatever those are, to call them a private business is an abuse of the English language. They are some amalgam of public, private, under the thumb of the administrative state. And more and more of these companies that exert power over the economy have this flavor to them. And I think this binary view is not useful anymore.

Bill Walton (00:13:59):

Well, let's real quick do a big definition of the administrative state, because I think a lot of people who have been listening, watching the show, know that's a theme, but we really need to say what it is. I mean, the constitution came up with this notion of the executive branch, the judicial branch and the legislative branch, and I guess we had the fourth estate, which was the press.

(00:14:20):

But now what's happened is Congress has delegated so much power to the administration, to all the agencies, whether it's the SEC or the Fed or commerce department or whatever, that now, instead of laws coming out of... And professor, correct me if I'm not getting this right. Now, instead of laws coming out of Congress, the regulations, laws disguised as regulations, are coming out of these agencies. Is that the administrative state?

Todd Zywicki (00:14:51):

Yeah, I would go even further.

Bill Walton (00:14:56):

Okay, let's do it.

Todd Zywicki (00:14:56):

So as you said, we've got legislative and we've got executive and we've got judicial. It's possible, there is something called administrative law that is theoretically possible to be consistent with the rule of law, where the government actually does follow some regularized procedures for making administrative regulations and the like.

(00:15:23):

And interestingly enough, the modern discussion over the rule of law, originally with AV Dicey in Britain, who wrote his book in the late 19th century on the rule of law specifically to address the need for the rule of law to apply to the administrative law that was being created at the time.

(00:15:43):

What we see today, and what I would consider the administrative state, essentially bears no resemblance to law in any meaningful sense, which is what we see going on in the financial system. What we see going on more and more is not anything that looks like regularized law of promulgation of regulations, notice and comment rulemaking, where they seriously take critiques seriously.

(00:16:06):

And dude, what it is is this process of what Wayne Cruz, I like his, from the competitive enterprise institute, calls it regulatory dark matter, which is the stuff that's not really even law, but has, everybody knows, that binding effective law. So that's the guidances and the supervision and the dear colleague letters, if you remember that one from the Department of Education during the Obama administration. Or as John Allison calls it, the regulation by raised eyebrow, which is, do you really need to do that? Or the threats or the cajoling, and all this sort of stuff, which is all backed by the threat of government action or government inaction, which is, so many times now, you just need government permission to be able to do something for a merger or a permit or whatever the case may be.

(00:17:00):

And the government can just passively aggressively punish you. I mean, we know, for example, there's situations, and when there's new financial regulations come out, and no bank will be willing, even though it costs them a lot of money, no bank's willing to challenge it. Why? Because they're afraid of retribution from their regulators, which is of course illegal.

(00:17:21):

But everybody knows that it happens across the economy. And so when I talk about the administrative state, that's what I'm talking about, is they've got their fingers in everything, and it's this soft power. It's this power beyond law that I talk about in my article, about how we need to start taking this seriously and thinking about how we tame this.

Bill Walton (00:17:42):

And they're also sneaky, because you read about this, I think it was, I'm getting into geek land, UDAP, which is unfair, deceptive and abusive practices, and that's code for disparate impact people. They just sort of arbitrarily decide, you can't do this or you can, depending on whether you're in a favorite group. And didn't somebody sneak this into a 2000 page supervision and examination manual?

Todd Zywicki (00:18:17):

This is exactly right, Bill.

Bill Walton (00:18:18):

Isn't this exhibit A for what you're talking about?

Todd Zywicki (00:18:20):

Exactly. This is the class. This is a great example.

Bill Walton (00:18:23):

Let me just hold you. This is Bill Walton show. I'm with Todd Zewicki, professor of George Mason, soon to be an anti progressive in Boulder. And we're talking about the administrative state, and really how sneaky they are, and how we really ought to be aware of what they're up to, and pay a lot more attention than we are.

Todd Zywicki (00:18:43):

And this is a great example of what you're saying, Bill, which is, this is something that came from the Consumer Financial Protection Bureau, and we have on the books something called the Equal Credit Opportunity Act, which has been law for a very long time, that provides rules and standards to prohibit discrimination against protected classes with respect to the grant of credit. And that's been what it's been for a long time.

(00:19:11):

We also have, for many, many years something called the unfair and deceptive acts and practices from the FTC, and other regulators have had this, and never before, in the decades in which these two things have existed, have we thought that unfair deceptive acts of practices includes all the discrimination stuff that we see in ECOA.

(00:19:35):

And so what the CFPB has conjured up is this idea that, in fact, UDAP, which is basically the same, just with the abusive as well, because they're promulgating this under the unfairness prong, UDAP actually prohibits discrimination in anything related to financial services.

(00:19:54):

So you have more overdraft protections, more overdraft charges, for one category of people than another. It takes longer to the answer the phone or whatever the case may be, could potentially be this.

Now, there's no way this could survive scrutiny under a standard sort of notice and comment rulemaking, right? There's no basis for it. So there's no legal basis for it. There's no factual findings to support it, anything like that.

Bill Walton (00:20:24):

So if it goes through the regular process of law-

Todd Zywicki (00:20:27):

It would never survive. It would take years and it would never-

Bill Walton (00:20:30):

That's our headline here, is the rule of law, or is it not?

Todd Zywicki (00:20:33):

Yeah, right. There's no way a court would uphold this, given this history that I described. It's clear that this doesn't cover this. So they didn't decide to use notice and comment rulemaking. They could try to do an enforcement action, but of course, if you do an enforcement action, then you have due process protections. You could challenge it in court. They would almost certainly get a stay, whichever it was enforced against, for the same reason.

(00:20:58):

So what did the CFPB do? They've got this massive examination manual that's supposed to be just, here's how to comply with the law. They changed one paragraph in the examination manual to say from now on, unfair deceptive acts and practices includes this activity.

(00:21:16):

Now here's why this is so nefarious, Bill. This is why this seemingly trivial thing is so important, because this is a model that the Biden administration has used across the administrative state, which is, under their argument, the CFPB's argument, providing supervision is just good advice. Here's how you can comply with the law. And so they say, that's not a final agency action. We haven't made you do anything. You can't challenge that.

Bill Walton (00:21:44):

So you can't litigate.

Todd Zywicki (00:21:45):

You can't litigate it, right. Because they say it's just advice.

Bill Walton (00:21:48):

Wow.

Todd Zywicki (00:21:49):

It's very much like we're seeing with the Twitter files.

Bill Walton (00:21:51):

Wow, is that Orwellian.

Todd Zywicki (00:21:52):

Yeah, right, exactly. And so they say, you can't challenge it until we actually take an action. But everybody knows, because of the way the regulatory state works, and we'll talk about this more, is everybody understands that's really binding on a bank. A bank doesn't want to get crosswise with its supervisors. They don't want to be have this regulation by raised eyebrow because that just leads to more and more pain. So it effectively forces them to comply, even though technically they're not required to comply.

Bill Walton (00:22:28):

Well, let's spend a moment there about the banker and the regulators. It used to be the banker was [inaudible 00:22:36], and the regulators are up in Chicago, and regulators would come down every three months or six months for a few days for an examination, and they'd talk and things like that. Now though, particularly with the big banks, the regulators are on site full time.

Todd Zywicki (00:22:51):

That's right.

Bill Walton (00:22:51):

They've got offices, they've got conference rooms, they've got probably their own cafeteria. I don't know. No, but they're interrelated. So if you're a banker and you're sitting with the regulator, and the regulator says, "Well, I know it's not in the law, but you understand how this works, don't you?"

Todd Zywicki (00:23:08):

Right, right. No, that's exactly right. In the history of supervision, there's a reason why we have this supervisory or examination process, and it really goes back to deposit insurance and the logic of the... So this is why they call prudential regulation. Deposit insurance, love it or hate it. The logic of deposit insurance to protect depositors, but that creates a moral hazard problem for the banks, that the banks now can keep the upside and externalize the downside because most depositors won't pay attention to what's going on.

(00:23:48):

So in exchange for the government privilege of deposit insurance, you have to subject yourself to examination, to make sure you're not taking reckless risks. That has expanded now to cover all of this social agenda and all the kind of stuff that we see in this manual, the things that supervisors, examiners subjectively think create risks to you such as vague reputation risk.

Bill Walton (00:24:14):

Well, let's do history. Let's do a historical lesson. Because I think all of us, and when I came to the industry, I was sort of in this category, I sort of assumed that deposit insurance and regulators and doing what they're doing, they've been around forever. Well, they haven't been, and they've only been around since the thirties, right? Deposit insurance was when, 1932?

Todd Zywicki (00:24:34):

Around there. Yeah, right.

Bill Walton (00:24:35):

And before then, if you were a customer of a bank, before you'd put your money in that bank, you wanted to make sure that bank had capital, that bank had reputable people. They were ready to protect your money and get your money back to you if you needed it. So the market supervised the banks, and then after the Great Depression, they declared in their wisdom, well, now they had to protect depositors. So they did the deposit insurance, which was, I think, restored a lot of faith in the system.

(00:25:06):

But the trade was, they said, "Okay, well, the regulators are now going to determine whether banks are safe."

Todd Zywicki (00:25:11):

Correct.

Bill Walton (00:25:11):

And so they put all the power and all the oversight in the hands of the regulators. And those of us just going around putting money in banks are supposed to trust the regulators to oversee it. And since then, we've had banking crisis after banking crisis after banking crisis.

Todd Zywicki (00:25:28):

That's right.

Bill Walton (00:25:29):

And in the case of Silicon Valley, the regulators have been in there a few weeks before, and they said, "This bank is great. It's in perfect shape. There's no risk here. Their client compliance is great, their diversity, equity, and inclusion, they've got five people in that department."

(00:25:45):

But what they forgot to do is, they forgot to look at the balance sheet and the interest rate risk. So anybody counting on the regulators in the case of Silicon Valley Bank, well, on the other hand, then they didn't care about the deposit insurance there, did they? Anyway, amplifying that story. I don't want to steal all the-

Todd Zywicki (00:26:04):

No, that's right. Right. Which is, it goes, the Fed was early in the 20th century, and then during the Great Depression, we get this whole system with deposit insurance. And you described it perfectly, which is, deposit insurance... First, let me say, I understand the logic of deposit insurance. Depositors are... It's very complex. The financial system is very complex. Depositors are going to have trouble monitoring. There are free rider problems and the like, but deposit insurance, like any form of insurance, brings what economists call the moral hazard problem, which is, if you have insurance, you might act a little more recklessly.

(00:26:47):

And if you're a bank, the concern is, if you aren't being monitored by your creditors, you might act more recklessly. Now, as you said, the traditional approach to that was pretty straightforward, which is banks just held a lot of capital. They held capital reserves to make sure that they could make their creditors whole.

(00:27:08):

What happens after you get deposit insurance is now banks reduce the amount of capital, they have to hold because depositors don't insist on it. And the whole banking system becomes more unstable, because now you've reduced the amount of capital. Now you layer on top of this the problem you described, which is central planning, which is now the regulators are dictating what they think is risk, and God bless the federal regulators, but the people who are working as a low level employee and a federal bureaucracy, are they better than the people who are running banks and understanding what risk is, and understanding what best serves their customers and the like?

(00:27:55):

And so as you described, what we've seen since then is this, we've actually seen more instability in the financial system, going back to the savings and loan crisis, going back to the 2008 financial crisis. And I think over and over again, what we've seen is, a lot of this is created by the regulatory structure itself, for reasons I talk about in the paper. But I think one of my favorite lines from the debate over Dodd-Frank was when Congressman Jeb Hensarling said, "There are at least three unintended consequences on every page of this 2,400 page piece of legislation." So...

Bill Walton (00:28:33):

Well, and then he went to work in a big bank, but that was a good move for him, I think, personally. Well, the thing about banks is that you think about a depositor, big banks in particular are analyzable. I mean, you can't really look at their balance sheet of financial statements. I don't care how much disclosure you've got, they're impenetrable even for somebody who's trained in finance.

Todd Zywicki (00:28:58):

That's right.

Bill Walton (00:29:00):

And I'm not even sure the CEOs of the big banks understand their own balance sheet. I mean, it's almost humanly impossible to do it.

Todd Zywicki (00:29:07):

They're so complex and so opaque. That's exactly right. And we saw this coming out of the financial crisis. Some of the reports of board of directors, for example, and senior officials-

Bill Walton (00:29:18):

Don't get me started with the boards.

Todd Zywicki (00:29:19):

-trying to even have a clue as to what was going on down on the 42nd floor, where the guys on the 39th floor were selling subprime loans indirectly to the guys on the 42nd floor, right? Nobody knew what was going on, and the whole thing blew up so...

Bill Walton (00:29:35):

Anyway, this is Bill Walton. I'm here with Todd Zywicki, who is our resident guru in all things financial and regulatory, and delighted to have you here. We're just trying to get to the rule of law, and how it's come unmoored in finance. And we've described a lot of problems. I mean, is there a remedy, I mean, can we step... I mean, you pointed out in your article, it seems to me like Congress ought to reclaim its powers, is one of the big remedies. What do you...

Todd Zywicki (00:30:08):

Yeah. So there's two big questions, which is what do we want to do about it. But first I just want to amplify something we talked about earlier, which is this is important because, in many ways, the financial system is the apotheosis of the regulatory state. And again, what I mean by that is this thick blanket of complex regulation of sort of exchanging government favors for government interference.

(00:30:41):

Until I started looking at this, I was always confused as to why the Senate traditionally had the Senate committee on banking and housing and urban development, and I said to myself, what does banking have to do with housing and urban development? Well, now we know, which is, it's sort of the unholy alliance that we saw during 2008, which is that banks are basically expected to be off balance sheet slush funds for politicians and the like to do things like subsidize the housing market, which went so well in the run up to 2008.

(00:31:17):

So we've seen this intertangling of politics with the financial system. We see this discussion we've been having about supervision and the regulatory dark matter of the various ways in which the government can exert its power without ever writing anything down, for example, because banking is so heavily regulated and so entangled with these regulators, but it's just the prototype.

(00:31:46):

This is the model that the progressives are using to do the same thing, to basically evade the rule of law, to evade things like transparency, notice and comment rulemaking and the like. So this is why I think because it's the leverage point, both economically and as a political agenda, it's particularly important to think about how we can try to in some way or another constrain this.

Bill Walton (00:32:14):

Your article's a really great overview of this. We talked about the 2000 page manual that they slipped something into. They're also using, doing something obscure called the Basel Capital Requirements. And just to back up, Europe has got some, I guess Basel is in Switzerland, and that's where all the bankers are and they've got capital, the European Union has capital requirements, and they say for this type of loan or this type of asset, you need to hold these amount of capital against it.

(00:32:50):

And it's really pernicious because they've declared that loans to countries don't require any capital at all because countries are risk free. And so consequently, European banks have got like 75% of their loans to countries. And I'd argue the countries are riskier than a lot of multinationals, whereas in the United States, about 25% I think is government loans. But what they're doing is they're shifting capital requirements. So they're saying fossil fuels, if you've got loans to the fossil fuel industry, what are they doing there?

Todd Zywicki (00:33:29):

Yeah, this shows you, I was smirking as you're talking because it always just amused me that Greek bonds and German bonds are treated-

Bill Walton (00:33:40):

Greek bonds are the same risk.

Todd Zywicki (00:33:42):

Greek bonds and German bonds are treated the same in terms of their riskiness.

Bill Walton (00:33:46):

Makes the Greeks very happy.

Todd Zywicki (00:33:46):

Yeah, right, exactly. But obviously this is the danger of central planning, which is, if you could try to fix prices of bonds, and you're dealing with a profit maximizing sector, people are going to buy Greek bonds because they're cheaper if they can count the same as German bonds. But to your larger point, I think about Basel capital and the like, and we see this not just in banking, but also in the Securities and Exchange Commission rules involving climate change risk.

(00:34:18):

This is just a marvelous example of the nefariousness of the regulatory state and action. So here's what they do, which is, they say, basically, you have to hold an appropriate amount of capital for any risk. Now, what does risk involve? It involves economic risk, but what else does it involve? What they call political and transition risk. So what this says is, the way they basically gin this up is they say, "Well, there's always a risk out there that the government's going to do something stupid and ridiculous when it comes to fossil fuels, right? They're going to just ban fossil fuels or something like that, right?"

Bill Walton (00:35:00):

Well, that's an actual risk.

Todd Zywicki (00:35:01):

It's an actual risk, right. That's what I'm saying. It's an actual risk that the government will do something insane like trying to ban fossil fuels. So what they say is, "Well, the fact that the government might do that then-"

Bill Walton (00:35:12):

The government's telling you you need to hold more capital.

Todd Zywicki (00:35:14):

Then it makes the investments in fossil fuels riskier. So you have to have more capital against the fact, we're going to make you, over in the financial regulators, they're going to make you hold more capital because those lunatics over there in the environmental group might force you to destroy the value of these investments.

(00:35:37):

And so voila, what have you done? You've raised the cost of providing capital to the financial industry without the government actually doing anything, right? That's the thing, is you don't have to actually do anything. The financial regulators just have to decide this is an elevated risk. So you'll remember, this kind of disappeared without a trace, but you'll remember President Biden's first nominee for the office of the controller currency. The controller was, who can forget, Saule Omarova.

Bill Walton (00:36:04):

I can't pronounce her name. You pronounce her name.

Todd Zywicki (00:36:06):

Saule Omarova, right? And do you remember what got her tripped up was, she had said we should use the financial system to bankrupt the fossil fuels industry. And this is exactly how they would do it, completely non transparent to the rest of the world, is all they have to do is flip a little dial. The regulators have to flip a little dial that says this type of investment in fossil fuels is much riskier than this type of investment in alternative energy.

(00:36:36):

And all of a sudden, what have you done? You've driven incentives to shift investment away from fossil fuels to renewable energy and the like. And you've basically accomplished your goals without ever passing a regulation. And that's completely, almost every American is oblivious to the way that that process can work.

Bill Walton (00:36:58):

And if they're writing risk disclosures, and I've been through this with lots of prospectors, if they're intellectually honest, they would say green energy, alternative energy, is very risky because it depends on government subsidies. And guess what? The trillion dollars of government subsidies might run out someday because we can't afford it. So you've got risks in that, that they're not forcing you to disclose, but they are in this bizaro world of risk. Well, they might put fossil fuels out of business, which is what they're trying to do.

Todd Zywicki (00:37:34):

That's right. And the Securities Exchange Commission, in this proposal they have for disclosures on so-called climate risk includes the same thing.

Bill Walton (00:37:41):

Well, this is Gary Gensler, SEC, once again, arbitrary. He runs the SEC, he's the chairman, I guess I understand that the chairman has a massive staff, and the other four commissioners have a secretary.

Todd Zywicki (00:37:53):

Basically, yeah, right?

Bill Walton (00:37:55):

So he runs everything.

Todd Zywicki (00:37:56):

He runs everything.

Bill Walton (00:37:56):

Arbitrary [inaudible 00:37:58], and he declared that companies were going to have to disclose massive amounts of climate risk.

Todd Zywicki (00:38:03):

Right. Including the so-called transition risks. And the point is, under the securities exchange laws, you're only supposed to disclose risks that are material to the financial condition of the company. Clearly, none of this is material to the financial condition of the company. Clearly what it is is designed to be a way of forcing companies to basically disclose information that activists can use against them, and allow them to get action to this, and basically browbeat them and use informal pressure basically to do this, and just, again, raise the cost of dealing with traditional energy, and shift to other things that are more politically favored.

Bill Walton (00:38:53):

So I want to shift gears. I want to get into central bank digital currency, because that to me is the biggest single thing looming on the horizon. But before we jump into that, how would you... For those, I mean, I'm more deeply in this wonk stuff, as are you, but for somebody that's not really a finance professional or somebody in the industry, how would you frame how people ought to be thinking about this, and what they ought to be telling their congressmen to do?

Todd Zywicki (00:39:25):

Yeah, great question. I was thinking about this, how to sum this up. Back during the socialist, communist planning days, the idea was is that the central planners of the government get ahold of the so-called commanding heights of the economy, which were steel, telecommunications, energy, and the like. Well, nowadays, the commanding heights of the economy are finance and social media. And so what we see here, the way to people to think about this is that finance, more than anything else, is the centrality of our lives, which is, you can't have a business without a bank account. You basically can't live without a bank account.

(00:40:13):

And so what the progressives have come to understand is, you can use this access to the financial system as a lever, not just to infringe on people's ability to bank, but infringe on their ability to live, right? And so if you can take somebody's bank account away and basically put them on, if you've listened to the tape of Mike Lindell, who you mentioned earlier, where the bank tells Lindell, "We don't have to put you on-"

Bill Walton (00:40:39):

I did listen to that tape.

Todd Zywicki (00:40:41):

Right. "We don't want to have to put you on the bad boy list." Do you remember that? He said, "You know, you can..." Basically what they said to Lindell is, "Look, you've got two options. You can voluntarily close your bank account or we will close your bank account involuntarily, and if we close your bank involuntarily, we'll put you on the 'bad boy list', which is not quite clear what that is, although I think I know what it is, and then that means you're not going to get a bank account anywhere else."

(00:41:05):

And so to say he voluntarily closed his bank account at that point is silly to say, but that's the sword of Damocles. That's exactly what the social media companies like Twitter did to people with the first strike and the second strike and the third strike, which is that, what they want to do is chill you from expressing certain opinions and the like.

(00:41:31):

That's a sense of which to say, this is the commanding heights now, which is getting your fingers into the financial system allows you to control every part of people's lives now, potentially, through de-banking them, as we talked about, by controlling the flow of capital and the like. And I give the example, which is not fanciful. I give the example in the paper of the Canadian truckers, if you remember them, when they were protesting, and Trudeau froze their bank accounts, and then they switched to cryptocurrencies and they froze their cryptocurrency wallets and tried to steal it.

(00:42:12):

Why? Because they said that they were all involved in basically conspiracy to break the law, through sitting in their trucks there and honking their horns too much. Well, think of it this way, Bill, which is, the Southern Christian Leadership Conference, led by Martin Luther King in the 1960s, were doing the exact same thing as the truckers. They were accused at the time, and this is why they were arrested as part of their protest, they were accused of basically engaged in a conspiracy to engage in trespassing, disturbing the peace, right? Those sorts of things.

(00:42:45):

Now, imagine if the regulators at the time had said, "We're not going to allow people to donate money to the Southern Christian Leadership Conference anymore because they're using this to engage in a conspiracy to break the law intentionally. We're not going to allow you to use," as they did with one of the leaders of the Canadian truckers, "You have a right to bail in this country, but you don't have a right to access your bank account to post bail because that's ill-gotten money. So you can have a right to bail."

(00:43:16):

But if you can't post bail, what good is it? And this is why it seems conspiratorial. It seems crazy to think that banking is so important to this, and finance is so important to this, but this is why I think it is really the linchpin of everything we think of as being able to live as free people, not just economically, but to express our opinions and everything else.

Bill Walton (00:43:45):

Cryptocurrency. Somebody was saying to me, "Well, that couldn't happen." And I said, Well, it did happen in Canada. How did they get away with that?" Somebody said, "Well, the crypto is away from the government." I don't think crypto is all that away from the government.

Todd Zywicki (00:43:59):

No, that's what they said, right? And so I'll tell you, unfortunately I was not surprised by what happened, and a lot of our libertarian friends had been telling me the same thing, and I was always skeptical. So let me tell you why my skepticism was warranted, again, because of the way the modern administrative state works.

(00:44:18):

So the logic is that crypto is anonymous. And so the idea would be you're outside the banking system, your crypto wallets are basically anonymous. You have to have these numbers to unlock it. But the key is you essentially still have to have something like a crypto bank or crypto wallet. Why? Because the Kroger and the Harris Teeter still aren't taking cryptocurrency. So if you want to buy groceries or pay your rent or whatever, at some point you have to convert your money from crypto back into dollars, or pay your bail, for example.

(00:44:57):

And so their view was it was all anonymous and these things, and so nobody would know who had what, but what the Canadian government did is exactly, exactly what I predicted they would do. They would say, "We don't know who those wallets are. You don't know who those wallets are," but here's what they said. They said, "From now on, we are going to make you, the crypto company, responsible for knowing whose wallet it is, and it will be a violation of the law in and of itself for you to have clients that you don't know who they are."

(00:45:39):

And so basically what they're doing is extending the principle of anti-money laundering laws and the like, and basically putting the onus on the company to force you, as a condition of business, to reveal yourself. And so this is why the libertarians, who are sort of crypto utopians, have missed the point. Because they don't understand how the regulatory state works, which is, we may not be able to figure out who it is directly, but we can force you, under the threat of imprisonment, and tell you if you deal with people and you don't know who they are, then you are the one who is in hot water. Does that make sense?

Bill Walton (00:46:24):

Oh yeah.

Todd Zywicki (00:46:24):

So that's how you create a regulatory crime out of thin air. And what we've seen now in the United States, it's been called now Operation Choke Point 2.0, right? We talked about Operation Choke Point under Obama, which targeted payday lenders and the like. But there's reports now about Operation Choke Point 2.0, which is crypto companies are being de-banked. I have a colleague who was going to start a little nonprofit research organization to study cryptocurrency. He has been turned down by six banks to create a bank account for his little research organization because it contains the word crypto in the title of the thing. Now, why is crypto the new target of the left?

(00:47:12):

It's for exactly what you're saying, which is they want to get ahold of crypto, they want control it, and to the extent they can, so here we'll illustrate the point. Rashida Talib, the congresswoman who's one of the squad along with AOC and those, do you know what the first bill she proposed when she came to Congress was? A bill that would require cryptocurrency to be in stable coins, to be within the banking system. And she claimed it was to protect consumers. We all know what that is, is they want to sweep cryptocurrency into the banking system precisely so that they can control it.

Bill Walton (00:47:50):

Isn't it interesting how the squad's become part of the deep state so rapidly? I mean, there's no more deep state notion than that [inaudible 00:47:57] AOC defending Hunter Biden.

Todd Zywicki (00:48:00):

Yeah. Yeah.

Bill Walton (00:48:01):

I mean it's really...

Todd Zywicki (00:48:05):

They've discovered that the deep state and the administrative state is their ally.

Bill Walton (00:48:08):

Oh yeah. Well, let's do one big last hurrah on deep state issues. It's Todd Zywicki. I'm Bill Walden. I'm with Todd Zwicky, and we're talking about all things financial, and why we need to concern about the government and our money. In particular right now, August, 2023, we very much need to be concerned about the Fed's plans, and they're rolling it out as we speak, for Central Bank digital currency.

(00:48:40):

And this is the one thing, this would be a game changer if that thing rolls into place. It would give them pretty much complete control over all of our spending. And the SEC has a similar plan on disclosure of our investible assets and all our assets, in fact. And so talk about the totalitarian, the end game is through the banking system, and through the investment portfolios we have. But you mentioned something in your piece. And by the way, where can we find the piece? We're going to have it on our website-

Todd Zywicki (00:49:15):

The Heritage Foundation, First Principles. Yeah, the Heritage Foundation.

Bill Walton (00:49:17):

But we'll have it on our site and it'll be... You can link it and find it, it only takes about 45 minutes to read. You'll know a lot you feel like you should have already known after you've read it. I did. But you threw a word in there. Central Bank digital currency, programmable.

Todd Zywicki (00:49:34):

Yeah.

Bill Walton (00:49:36):

What's that mean?

Todd Zywicki (00:49:37):

Yeah. And so programmable Central Bank digital currency would allow them to... It's just bits, right? It's just stuff that appears in your bank account electronically.

Bill Walton (00:49:50):

So honestly, my bank's now not at PNC. My bank is the Federal Reserve Bank of Richmond.

Todd Zywicki (00:49:55):

So it could be that you get it directly through the Fed, which is one of the proposals. Or it could be that it is intermediated through a private bank. But basically, the way it works is, think about, for example, food stamps. Food stamps can only be spent on certain goods. In that sense they're analog, but they're programmable in some sense. What they could do is they could give you central bank digital currency instead of real dollars and say you can only spend it on this, that, or the other.

(00:50:31):

So they could say, "You can only spend so many credits on gas this month, because you've exhausted your fossil fuel amount." You could program it that says, we're going to say that this certain amount of money can only be spent on minority owned businesses.

Bill Walton (00:50:50):

So that little flag on the tank at the pump, at the gas station, which limits your spending to a hundred dollars, which became archaic during Joe Biden's run up and gasoline prices, that would be in your credit card. So it's not just to limit at the gas pump, but that'd be in your credit card, where this month you spent $600 on gasoline. That's way too much. So you can monitor people's carbon footprint through how much they spend on gas.

Todd Zywicki (00:51:21):

That's right. Gas or the kind of things they spend it on. You could control if you thought they were, the government has a way of leaking information pretty readily now, so if you spend money on the wrong sort of reading materials, you can imagine all that.

Bill Walton (00:51:37):

Or you couldn't spend money at a cake shop that refused to bake cakes for a gay wedding.

Todd Zywicki (00:51:42):

That's right. For example, right.

Bill Walton (00:51:43):

So you couldn't use your money there.

Todd Zywicki (00:51:44):

That's right. That's right.

Bill Walton (00:51:46):

So you can put them out of business.

Todd Zywicki (00:51:47):

And it's funny, Bill, I mean, I kind of came to this after following the de-banking, and it sounds-

Bill Walton (00:51:54):

You're talking about something-

Todd Zywicki (00:51:55):

It sounds like, the joke now is, what's the difference between a conspiracy theory and reality? About three months.

Bill Walton (00:52:03):

You said that eight months ago, and nine things have happened since you were last here.

Todd Zywicki (00:52:12):

That's right. That's right. And so I think that the lesson here is that now that we don't have the rule of law, we do not have anything. We don't have the rule of law here anymore. And so I think what that means is, we must always be wary of the principle, the small incursion. We must always be wary of the principle. Now, I say that from looking at the financial system.

Bill Walton (00:52:35):

What do you mean be wary of the principle? What does that mean?

Todd Zywicki (00:52:38):

That basically, if you give the government an inch, we should assume they'll take a mile. That if you allow a small exception, the exception will expand. They've done this with social media. They took the small exception for violence and harassment, that sort of thing, and then turned it in this misinformation thing.

(00:53:00):

That's what they do here. And I say this both from studying the financial system, but also from being a professor for 25 years. Everything we're seeing going on in society, we saw this 20 years ago in academia, and everybody said, "Oh, that's just academia. That's not going to happen anywhere else." And it did, right?

(00:53:16):

The principle, the small principle embedded in the small little idea will expand. And so I think what we have to accept is, if you think that the government should be able to freeze people's bank accounts because they don't like the Canadian truckers, we should assume that's going to just become a general power that they can wield. And keep in mind, because [inaudible 00:53:42], 65% of American Democrats agreed with Justin Trudeau's action in freezing those bank accounts.

(00:53:50):

And so the point here is, it seems kind of crazy, but I think we need to be aware that this is why these people want Central Bank digital currency so much, which is, they claim that they want to be able to control drugs, human trafficking, all that sort of stuff. More power to them, right? That's bad stuff. But here's the problem, is that that's always the camel's nose under the tent, right? Operation Choke Point was justified by the fact that, well, we're just trying to prevent fraud.

(00:54:24):

It went from preventing fraud to preventing payday lending and gun shops. Here you can justify CBDC, and this is why I say you've got to be aware of the principle, which is, I think it would be a great thing if we had some way of controlling human trafficking, illegal activity, money laundering and that sort of thing in a world where we had the rule of law and we could trust our regulators to limit it to that discretionary power. That would be a good thing to have.

(00:54:54):

But in the world we live in now, I think it's naive to believe that if we grant them that power for that limited purpose, that it's going to stay reserved to that power. And a lot of people point out that there is no legal authority for the Federal Reserve to do this. And I think what they've shown again and again and again over recent decades is, they're not sitting around waiting for legal authority. They just do it. And after it's a fait acompli, it never gets undone.

Bill Walton (00:55:23):

Well, so the remedy is to get Congress to prohibit it.

Todd Zywicki (00:55:30):

Yes.

Bill Walton (00:55:30):

How are we going to do that through the Senate? How are we going to get Joe Biden to sign that into law?

Todd Zywicki (00:55:34):

So that I think is more general-

Bill Walton (00:55:36):

So this ought to be a campaign issue in the 2024 presidential campaign.

Todd Zywicki (00:55:42):

That's right.

Bill Walton (00:55:42):

If we have enough time.

Todd Zywicki (00:55:43):

Yeah. And Ron DeSantis has in fact put this proposal out there, right? To formally ban Central Bank digital currency. I think he may have actually banned it in Florida. But this is the point, and it takes us all the way back to where we started, Bill, which is the rule of law and the public private distinction, which is, a lot of people say, "Well, we don't need to worry about Central Bank digital currency because the Fed doesn't have that power granted to it."

(00:56:09):

But that's not the way the regulatory state works these days, which is, basically, it expands to fill the void. So unless it's specifically prohibited, they're going to act as if it's permitted, right? And that's what we see over and over again, which is, unless it's specifically prohibited, they'll act like it's permitted.

(00:56:31):

So whether it's specifically banning Central Bank digital currency so that they can be sued immediately if they do it, whether it is, I argue, the fair access to financial services rule, that Brian Brooks issued from the Office of control of the currency, which would affirmatively prohibit discrimination in bank accounts based on political views, or affirmatively prohibit discrimination against fossil fuel companies and the like.

(00:56:58):

I think what we have to actually realize is that the administrative state has slipped its leash, that simply not granting a power is not enough. I think we need to more and more dictate limits on its power, prohibitions on the power of regulators, not just assume that if we don't grant them the power, they won't act.

Bill Walton (00:57:20):

So the big issue, the big takeaway is, we need to be mindful that the administrative state can do all this stuff, and instead of just passively writing papers or giving speeches, we need to get Congress to act with specific laws prohibiting this.

Todd Zywicki (00:57:37):

That's my view. And that's a peculiar position, I admit, for a libertarian.

Bill Walton (00:57:43):

Why is that peculiar?

Todd Zywicki (00:57:44):

Well, to impose-

Bill Walton (00:57:46):

For somebody who writes papers, I suppose.

Todd Zywicki (00:57:49):

Well, to call for more-

Bill Walton (00:57:49):

It's an excellent paper.

Todd Zywicki (00:57:52):

To call for more government laws.

Bill Walton (00:57:53):

Well, yeah, but you got to play the game. We've got to play the game as it exists.

Todd Zywicki (00:57:58):

That's right. And this is exactly right, Bill, which is in the world of the first best, we would live in the world with the rule of law. We don't live in that world. And so we are in the world of the second best. And so pretending like we still live in the world of the first best, I think is just naive.

Bill Walton (00:58:16):

Precisely.

Todd Zywicki (00:58:18):

So I think we need to take markets and politics the way they are in the real world and actually deal with that reality, rather than pretending like we still live in the 18th century world of Adam Smith and David June, and pretending like there's these easy solutions to these problems.

Bill Walton (00:58:40):

Okay, Todd, this is great. Todd Zywicki, now with Scalia School of Law, soon to be Boulder, University of Colorado in Boulder. I think I want to come sign up for your class on both the Rule of law and for Hayak, it's going to be an entertaining semester. I'm envious of the students out there. Anyway, thanks. And I may bring you in via Zoom at some point, as we get an emergency situation on this CBDC.

(00:59:10):

This has been the Boo Walton Show. Todd Zywicki's one of my favorite guests, back talking about the administrative state and finance, et cetera. Hope you enjoyed it, even though a lot of what we talked about was alarming and stuff we need to know about, and be lining up lines of action to do something about it. As always, you can find the show in all the major podcast platforms and on Rumble and on YouTube and Substack.

(00:59:35):

On CPAC now, on Monday night, we're starting up something new called Insider Access Live, which is where I'll be doing a Zoom show with anybody who would like to sign up and participate. And it'll be, I think, a fairly lively Q&A about this topic, and all the other topics we've covered in the show. And you can find that on our website. Simple form, fill it out, email address, we'll send you some notifications, and hopefully you will join us.

(01:00:03):

So thanks for tuning in and we'll be back.

Speaker 5 (01:00:08):

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