

Articles

SPECIAL INTEREST GROUPS LEGISLATION AND THE JUDICIAL FUNCTION: THE DILEMMA OF GLASS-STEAGALL

By
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I. INTRODUCTION

This article examines and analyzes the Glass-Steagall Act¹ (the Act), which separates commercial banking from investment banking and concludes that the most plausible explanation for the passage of the Act derives from a theory that recognizes the role of special interest groups in influencing legislative outcomes.² It follows ineluctably from the application of this theory to the Glass-Steagall Act that judges, when called upon to interpret the Act,

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¹ The Glass-Steagall Act is the popular name of ch. 89, 48 Stat. 162 (codified as amended in scattered sections of 12 U.S.C.), officially designated the Banking Act of 1933. See 12 U.S.C. § 227 (1976). The sections of the Banking Act that deal with the separation of commercial and investment banking are 16, 20, 21, and 32. These sections are "usually the intended reference when the name Glass-Steagall is used." Note, *A Banker's Adventures in Brokerland: Looking Through Glass-Steagall at Discount Brokerage Services*, 81 MICH. L. REV. 1498, 1501 n.12 (1983). For more general discussions of the Act, see Perkins, *The Divorce of Commercial and Investment Banking: A History*, 88 BANKING L.J. 483 (1971); Pitt & Williams, *The Glass-Steagall Act: Key Issues for the Financial Services Industry*, 11 SEC. REG. L. 234 (1983).

² An impressive literature has developed on the phenomenon of legislation that is the product of a bargain between some industry, trade or other special interest group and the legislature. Much of the literature can be traced to Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3 (1971). See also Aaronson, Gellhorn & Robinson, *A Theory of Legislative Delegation*, 68 CORNELL L. REV. 1, 39-55 (1983) (candidates form policy programs around identifiable group preferences); Jordan, *Producer Protection, Prior Market Structure and the Effects of Government Regulation*, 15 J.L. & ECON. 151 (1972) (presenting empirical support for theory); Posner, *Theories of Economic Regulation*, 5 BELL J. ECON. & MGMT. SCI. 335, 344 (1974) (economic regulation serves the private interests of politically effective groups).

will face a virtually insurmountable burden³ due to the vast dichotomy between the ostensible legislative intent and the actual motivations of Congress.⁴

In order to demonstrate this thesis, the article first examines the language of the Act as well as the formally articulated legislative intent. These purported justifications for the law are rejected. The article next describes the phenomenon of special interest group legislation and considers whether this theory can better explain the Glass-Steagall Act. The article concludes (consistent with a theory of the behavior of special interest groups)⁵ that the actual motive behind the passage of the Act can only have been that of protecting one group — investment bankers — at the expense of another — commercial bankers.

The article, within the context of the proffered theory, also considers the appropriate judicial response to such a statute. Since there is no basis to legally distinguish or question the legitimacy of statutes passed at the behest of special interest groups from other kinds of statutes,⁶ it would seem therefore that the judicial re-

³ This burden consists of finding a dividing line between investment banking and commercial banking transactions, when, in fact, the distinction between these activities is more apparent than real since the substance of both transactions is the same. Consumers see the products of commercial and investment banking as near perfect substitutes for one another. The consumers of these products are borrowers. These borrowers may obtain money by selling stock (i.e. purchasing the services of an investment bank) or negotiating a loan with a commercial bank. The consumer's decision between these alternatives is based entirely on price. See *infra* text accompanying notes 24-31. A survey of the major cases under the Glass-Steagall Act demonstrates, quite predictably, that because of these special problems inherent in special interest legislation there is virtually nothing left of the distinctions Glass-Steagall was designed to create.

⁴ The dichotomy between motive and intent in the interpretation of legislation has been developed in both the legal and the economics literature. See, e.g., Landes & Posner, *The Independent Judiciary In An Interest-Group Perspective*, 18 J. L. & ECON. 875, 879, 894 (1975) (judges utilize considerable interpretive leeway to rewrite legislation); Posner, *Economics, Politics, and the Reading of Statutes and the Constitution*, 49 U. CHI. L. REV. 263, 272 (1982) ("in reviewing a statute, courts are to look to the intent but not to the motive of the enacting legislature"). The legal literature has focused primarily on constitutional cases. See Brest, *Palmer v. Thompson: An Approach to the Problem of Unconstitutional Legislative Motive*, 1971 SUP. CT. REV. 95; Ely, *Legislative and Administrative Motivation in Constitutional Law*, 79 YALE L.J. 1205 (1970); Ely, *The Centrality and Limits of Motivational Analysis*, 15 SAN DIEGO L. REV. 1155 (1978).

⁵ See *infra* notes 54-61 and accompanying text for a description of this theory.

⁶ See *infra* text accompanying notes 64-66 for a description of other kinds of statutes.

response to all statutes should be the same. Courts, at least with respect to statutory law, are simply the agents of the legislature and must execute its will when considering clearly constitutional statutes. It follows that the proper discharge of the judicial function often will consist of enforcing a deal forged between the legislature and some interest group.

As consideration of the Glass-Steagall Act clearly demonstrates, one can predict that courts will inevitably have special problems when faced with special interest group legislation that are not present in other cases. Foremost among these problems is the dichotomy between legislative intent and legislative motive that is frequently the hallmark of a special interest group statute. Faithful interpretation of the statute in accordance with its purported (as opposed to actual) objectives is virtually impossible due to the intrinsic incoherence of the legislative mandate. Moreover, it is often beyond the capacity of the courts to delve into the legislatures' actual motives when construing pure special interest group legislation.⁷ As the analysis of Glass-Steagall will show, another problem that courts face when dealing with such legislation is interpreting the actions of the administrative agencies that intercede between the courts and the special interest groups.

The thesis of this article concerning special interest group legislation is highly relevant to the most important current Glass-Steagall controversy — commercial bank underwriting of commercial paper. The United States Supreme Court will review in the 1984 term the legality of commercial bank commercial paper activity.⁸ The Court's final decision with regard to the legality of commercial bank underwriting of commercial paper will have a significant impact on the structure and functioning of the financial markets.⁹ This clearly can be seen by noting the role of commercial paper in the market. Commercial paper consists of short term (average maturity of less than nine months) promissory notes issued by large

⁷ See Posner, *supra* note 4, at 272-73.

⁸ A.G. Becker v. Board of Governors of the Fed. Reserve Sys., 693 F.2d 136 (D.C. Cir. 1982), *cert. granted sub nom.* Securities Indus. Assoc. v. Board of Governors of the Fed. Reserve Sys., 104 S. Ct. 65 (1983).

⁹ N.Y. Times, Oct. 4, 1983 at D1, col. 2.

financial and industrial corporations.¹⁰ As such, the commercial paper market is in direct competition with commercial bank loan departments as a source of credit to top industrial borrowers.¹¹ Thus, if commercial banks are forbidden by the Glass-Steagall Act from participating in this lucrative line of business, they may see their share of the financial service market erode dramatically. Investment banking firms currently engaged in the buying and selling of commercial paper therefore do not want commercial banks to enter this lucrative field and possibly capture their share of the market.

But the "commercial paper case," as this litigation has come to be called, is important for another, more general reason. The case, and indeed the Glass-Steagall Act itself, represents a striking example of the effects of the independent judicial process on the "deals" struck between special interest groups and Congress and thus may have, by analogy, a considerable impact on the ability of the parties to enforce these deals. The conclusion of this paper is that the judicial process places severe costs and, indeed, perhaps general constraints on the efficacy of such deals. In sum, the case may well determine whether there *is* a Glass-Steagall Act anymore or whether it has been completely eviscerated by judicial interpretation.

II. THE GLASS-STEAGALL ACT

A. *Genesis*

Congress, like much of the general public, placed much of the blame for the great Depression squarely on the shoulders of the nation's commercial banks.¹² Prior to 1933, commercial banks engaged in a wide array of securities activities through so-called bank securities "affiliates." According to Congress, these affiliates "made one of the greatest contributions to the unprecedented disaster which has caused this almost incurable depression."¹³ Congress,

¹⁰ Hurley, *The Commercial Paper Market*, 63 FED. RES. BULL. 525 (1977); Note, *The Commercial Paper Market and the Securities Acts*, 39 U. CHI. L. REV. 362, 363-64 (1972).

¹¹ J.P. Judd, *Competition Between Commercial Paper Markets and Commercial Banks* 39, 48 (Staff Paper, Federal Reserve Bank of San Francisco).

¹² S. REP. NO. 77, 73d Cong., 1st Sess. 1 (1933).

¹³ 75 CONG. REC. 9887 (1932) (remarks of Senator Carter Glass, principal drafter of the

when reviewing the economic carnage left by the Crash of 1929, did not tarry over the question of whether or not it should limit the scope of commercial banks' activities. Rather, the debate centered on whether commercial banks' investment banking should be prohibited outright or merely regulated.¹⁴ Congress chose prohibition, *i.e.*, outright separation of functions, on the stated theory that the mere existence of commercial banks' securities operations, no matter how carefully and conservatively run, is inconsistent with the best interest of the bank as a whole.¹⁵ The nature of the debate makes it plain that the commercial bankers, who stood to suffer from an outright prohibition of certain of their activities, were in a very weak political bargaining position. Since, as the debates clearly show, Congress blamed these institutions for the Depression, it was a perfect opportunity for another interest group, namely investment bankers, to profit at their expense. The result of the congressional action, the Glass-Steagall Act, sought to achieve the complete separation of commercial and investment banking.¹⁶ In other words, the Act is the "Maginot Line"¹⁷ of the financial world.

B. *The Mechanics of the Separation — The Legal Maginot Line*

The foundation of the Glass-Steagall Act consists of sections 16¹⁸ and 21.¹⁹ Section 16 prohibits national banks from underwriting,

Glass-Steagall Act).

¹⁴ See *infra* note 15.

¹⁵ 75 CONG. REC. 9913 (1932) (remarks of Sen. Bulkley); Perkins, *supra* note 1, at 524-26.

¹⁶ Board of Governors of Fed. Reserve Sys. v. Investment Co. Inst., 450 U.S. 46, 61-62 (1981).

¹⁷ Bevis Longstreth, "Current Issues Facing the Securities Industry and the SEC," May 4, 1982 speech to the Securities Industry Association (*quoted in* Pitt & Williams, *supra* note 1, at 235.)

¹⁸ Section 16, codified as amended at 12 U.S.C. § 24 (seventh) (1976 & Supp. 1983), provides that:

The business of dealing in securities and stock by the [national bank] shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the [national bank] shall not underwrite any issue of securities or stock

¹⁹ Section 21, codified as amended at 12 U.S.C. § 378(a)(1) (1976 & Supp. 1983), pro-

selling and dealing in securities. Exceptions are made for municipal bonds and debt obligations of the United States government, as well as for purchases and sales "without recourse, solely upon the order and for the account of customers." Section 5(c) of Glass-Steagall makes the restrictions imposed by section 16 applicable to state-chartered banks that are members of the Federal Reserve System.²⁰

Section 21 complements the restrictions imposed on the power of lending institutions in section 16 by placing restrictions on the activities of investment banks. Any person "engaged in the business of issuing, underwriting, selling, or distributing, . . . stocks, bonds, debentures, notes, or other securities" is prohibited from engaging in the business of administering checking or savings accounts.²¹

Sections 20 and 32 of the Glass-Steagall Act contain the remaining ramparts of the Maginot Line separating commercial and investment banking. Section 20 forbids affiliations between banks and firms "engaged principally in the issue, flotation, underwriting, public sale, or distribution . . . of stocks, bonds, debentures, notes, or other securities."²² Section 20 was designed to prevent banks from engaging in investment banking activities in precisely the way they had engaged in such activities before the Act was passed — securities affiliates. Finally, section 32 prohibits an individual involved in any aspect of the investment banking business from serv-

vides that:

[It shall be unlawful] for any person, . . . or . . . organization, engaged in the business of issuing, underwriting, selling, or distributing . . . stocks, bonds, debentures, notes, or other securities, to engage at the same time . . . in the business of receiving deposits

²⁰ 12 U.S.C. § 335 (1976) provides that:

State member banks shall be subject to the same limitations and conditions with respect to the purchasing, selling, underwriting, and holding of investment securities and stock as are applicable in the case of national banks under paragraph 'Seventh' of section 24 of this title.

²¹ See *supra* note 19.

²² Section 20 is codified at 12 U.S.C. § 377 (1982). For an insightful discussion of section 20 and possible "loopholes" therein, see Bock, *The Glass-Steagall Act and the Acquisition of Member Banks by Unregulated Bank Holding Companies*, 100 BANKING L.J. 484 (1983).

ing as an officer, director, or employee of a national or state-chartered member bank.²³

C. *Economic Reality — Storming the Line*

Much of the controversy concerning differing interpretations of Glass-Steagall focuses on the definition of the term “security.”²⁴ Recently this definitional approach has been resolved by judicial inquiry into whether the commercial banking service in question is related to “traditional banking functions.”²⁵ This approach is inherently unworkable since it seeks to create a dichotomy *ex nihilo*. Obviously, the archetypal case of traditional commercial banking is a bank loan. On the other hand, buying and selling the common stock of a publicly held corporation is presumably the core function of an investment bank. But aren't the economic differences between these activities more apparent than real? A firm in need of capital may borrow it from a commercial bank or may obtain the money by selling stock. The firm will select the financing method that imposes the lowest net cost with all other things equal. Firms see these operations simply as alternative ways of obtaining funds.

Just as firms see borrowing money and selling stock as interchangeable methods of raising capital, investors perceive their decision as whether to deposit money in a commercial bank (by buying a certificate of deposit) or to purchase stock, based upon which transaction represents the highest net return. This point has been clearly articulated, albeit in a slightly different context: “In one

²³ 12 U.S.C. § 78 (1982); Board of Governors of the Fed. Reserve Sys. v. Agnew, 329 U.S. 441, 449 (1947).

²⁴ Karmel, *Glass-Steagall: Some Critical Reflections*, 97 BANKING L.J. 631, 633-34 (1980) (Glass-Steagall characterizes banking activity as permissible or impermissible on basis of whether a security is involved in the transaction); Plotkin, *What Meaning Does Glass-Steagall Have For Today's Financial World?*, 95 BANKING L.J. 404, 411 (1978); Note, *A Conduct-Oriented Approach to the Glass-Steagall Act*, 91 YALE L.J. 102, 102 (1981).

²⁵ See Board of Governors of the Fed. Reserve Sys. v. Investment Co. Inst., 450 U.S. 46, 56 (1981) (concluding that “services of an investment adviser are not . . . different from the traditional fiduciary functions of banks”). See *infra* text accompanying note 26. A.G. Becker v. Board of Governors of the Fed. Reserve Sys., 693 F.2d 136, 148 (D.C. Cir. 1982) (reviewing “traditional lending functions of commercial banks”).

sense every lender of money is an investor since he places his money at risk in anticipation of a profit in the form of interest. Also in a broad sense every investor lends his money to a borrower who uses it . . . for a price and is expected to return it one day."²⁶

If there is no real economic difference between a *loan* and an *investment*, then there is no real distinction between a traditional commercial banking function (lending) and a traditional investment banking function (buying stock), thus the difficulty of drawing the legal distinction. The Glass-Steagall Act does not contain a definition of the term "security." At one end of the spectrum, courts will have little difficulty categorizing such things as common stock, which has long been considered a "security," or at the other end of the spectrum, the extension of credit backed by a secured interest in real property, which has traditionally been considered a "loan." Congress, at the time it was drafting Glass-Steagall had distinctions such as these firmly in mind. Other investment vehicles, those that lie closer to the center of the spectrum, such as commercial paper, or shares in investment funds, defy such easy categorization.

The Securities Act of 1933²⁷ and the Securities Exchange Act of

²⁶ C.N.S. Enterprises v. G. & G. Enterprises, 508 F.2d 1354, 1359, (2d Cir.) *cert. denied*, 423 U.S. 825 (1975). This case went on to suggest that the "polarized extremes" of commercial lending and purchasing stock are "conceptually identifiable" on the basis of which party provides the "impetus for the transaction." *Id.* The court argued that in purchasing stock the impetus for the transaction comes from "the person with the money" whereas in the commercial bank lending context the impetus comes from "the person who needs the money." *Id.* This is demonstrably false. Often banks aggressively seek out corporate customers in order to loan them money. Commercial banks refer to their lending activities as "selling money." Similarly, sellers as well as buyers frequently provide the impetus for stock transactions.

²⁷ Section 2 of the 1933 Act, 15 U.S.C. § 77b, states in part:

When used in this subchapter, unless the context otherwise requires —

(1) The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, . . . or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

1934²⁸ both contain definitions of the term "security." The term is used in a "jurisdictional" context in both of these Acts. Therefore, courts must resolve the question of whether a certain activity violates these laws by first ascertaining whether or not such activity involved a security.²⁹ Although these Acts both contain a definition of the term "security," these definitions have been the subject of extensive judicial gloss.³⁰ Although at first glance it would seem that these decisions would shed light on the definition for Glass-Steagall purposes, the definition of "security" contained in the '33 and '34 Acts cannot be "borrowed" from these statutes and adopted for Glass-Steagall because the underlying congressional purposes for the Securities Acts differs from the congressionally articulated purpose of Glass-Steagall.³¹

²⁸ Section 3 of the 1934 Act, 15 U.S.C. § 78c(a), states in part:

(10) The term "security" means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a "security;" or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

²⁹ See, e.g., *Teamsters v. Daniel*, 439 U.S. 551 (1979) (whether noncontributory, compulsory pension plan constitutes a security dispositive in securities fraud case); *United Housing Foundation v. Forman*, 421 U.S. 837 (1975) (whether shares in nonprofit, cooperative housing complex are securities was dispositive in securities fraud case); *S.E.C. v. W. J. Howey Co.*, 328 U.S. 293 (1946) (whether interest in a citrus grove development was a "security" dispositive in injunctive action).

³⁰ *Id.* See also cases cited in Seldin, *When Stock Is Not a Security: The "Sale of Business" Doctrine under the Federal Securities Laws*, 37 BUS. LAW. 637, 637-38 n.2 (1982) (citing twelve recent cases construing "sale of business" doctrine); see *id.* at 639 n.7 (citing dozens of cases); see also Lipman, *Notes as Securities*, 14 REV. SEC. REG. 934 (1981); Schneider, *The Elusive Definition of "Security"*, 14 REV. SEC. REG. 981 (1981).

³¹ *A.G. Becker, Inc. v. Board of Governors of the Fed. Reserve Sys.*, 693 F.2d 136, 146 (1982) (no reason to assume Congress intended the term "security" to bear the same meaning in the different statutes); see Note, *supra* note 24, at 110 n.71.

D. *The Ostensible Legislative Intent*

*Investment Co. Institute v. Camp*³² is unquestionably the Supreme Court's most influential opinion construing Glass-Steagall. It has been called the Court's "first and seminal analysis" of the Act.³³ In *Camp*, the Court struck down a regulation issued by the Comptroller of the Currency authorizing commercial banks to operate mutual funds because the regulation was held to violate sections 16 and 21 of Glass-Steagall.

The mutual fund plan under review called for customers to tender between \$10,000 and \$500,000 to a commercial bank along with an authorization making the bank the customer's "managing agent."³⁴ In return, the customer was to be given "units of participation" expressing the customer's proportionate interest in the fund assets. These "units of participation" were freely redeemable and transferable.³⁵

The Comptroller had ruled that these "units of participation" were not securities within the meaning of the Glass-Steagall Act.³⁶ The Comptroller's contention was that this kind of bank investment fund simply makes available to the small investor the benefits of investment management that are available to large investors through the bank's trust department. The Court rejected the Comptroller's decision and held that the "units of participation" in the bank's fund were "securities" for purposes of the Glass-Steagall Act. In reaching its conclusion the Court recounted the "hazards" and "financial dangers" that arise when commercial banks engage in the activities proscribed by the Act.³⁷ In discussing these "hazards," *Camp* presents a lavishly complete presenta-

³² 401 U.S. 617 (1971).

³³ Ianni, "Security" Under the Glass-Steagall Act and the Federal Securities Acts of 1933 and 1934: The Direction of the Supreme Court's Analysis, 100 BANKING L.J. 100, 112 (1983). Actually *Camp* was the Court's second opinion interpreting the Glass-Steagall Act. The Court had previously decided *Board of Governors of the Fed. Reserve Sys. v. Agnew*, 329 U.S. 441 (1947) (interlocking directorates).

³⁴ 401 U.S. at 622.

³⁵ *Id.*

³⁶ 12 C.F.R. Pt. 9 (1970).

³⁷ 401 U.S. at 630 (citing congressional history).

tion of Glass-Steagall's formal legislative history. It is from analysis of this history that the gulf between the ostensible legislative intent and the actual legislative motive underlying the Act becomes clear. Each of the hazards described constitutes either (1) a legislative intention to ensure that commercial banks are held to a higher standard of care when making investments than investment banks (so-called safety concerns) or (2) a legislative intention that banks be held to a higher standard of care than other financial institutions when dealing with customers (so-called conflicts of interest concerns).

1. *Banks' Standard of Care When Making Investments*

The first hazard described was considered "obvious": that a bank might invest its own assets in frozen or otherwise imprudent stock or security investments.³⁸ It is hard to fathom how Glass-Steagall reduces the risks of banks making imprudent investment decisions. Perhaps Congress actually believed *all* investments in stock or securities to be inherently more risky than *all* other commercial banking activities. Actually, what is "obvious" is the fact that bank ownership of high grade, blue chip stock, which is prohibited by the Act, is inherently far less risky than many bank loans such as those to third world countries or to real estate investment trusts, to use modern day examples. A possible defense of the separation prescribed by the Act could be that *most* stock or security purchases are more risky than *most* personal or commercial loans. But the incoherence of this defense is apparent. It is just as likely that the opposite is true, *i.e.*, that most stock or securities are *less* risky than most bank loans.

Risk levels are reflected by risk premiums incorporated into interest rates. The higher the risk premium and rate of interest, the greater the risk of the investment, all other factors being equal.³⁹ The relevant characteristics of a portfolio are its expected return and its riskiness. Rates of return on stocks should be higher on

³⁸ *Id.*

³⁹ See generally J. LORIE & M. HAMILTON, *THE STOCK MARKET: THEORIES AND EVIDENCE* 172 (1973); H. MARKOWITZ, *PORTFOLIO SELECTION: EFFICIENT DIVERSIFICATION OF INVESTMENTS* (1959).

average than rates of return on commercial loans if such lending activity is somehow inherently "safer." There is no evidence that this is so. And, while commercial lenders — since they hold debt as opposed to equity instruments — are often in a better position in case of default, the greater liquidity of stock is a significant safety feature. Furthermore, the proscriptions of Glass-Steagall do not apply merely to banks' acquisitions, but to all securities — debt as well as equity. Clearly, if the relevant indicia of safety is the rate of return, by forbidding banks from diversifying their asset portfolios by holding stock, the Glass-Steagall Act makes commercial banking a riskier endeavor, not a safer one.

Besides this "obvious" danger to bank safety, the Court determined that the legislative history of the Glass-Steagall Act evinces a congressional concern with the "subtle hazards that arise when a commercial bank goes beyond the business of acting as fiduciary or managing agent and enters the investment banking business."⁴⁰ Several of these dangers can be described generally as a concern that banks will exacerbate bad lending decisions by "throwing good money after bad." *Camp* evinces a concern that a commercial bank would either invest in a particular company's stock or participate in the underwriting or promotion of such stock and then "make its credit facilities more freely available to those companies in whose stock or securities the affiliate has invested or become otherwise involved."⁴¹ In addition to lines of credit, Congress "feared that banks might even go so far as to make unsound loans to such companies."⁴² Moreover, just as banks might loan money to a corporation in order to bolster the value of the corporation's stock, so too might banks make loans to bank customers that customers would use to buy stock, thereby puffing up the price of the security.⁴³ If the loans were made with the "expectation that (the proceeds) would facilitate the purchase of stocks and securities,"⁴⁴ then a bank's efforts to manipulate stock prices would influence the bank to make bad commercial loans.

⁴⁰ 401 U.S. at 630.

⁴¹ *Id.* at 631.

⁴² *Id.*

⁴³ *Id.* at 632. *See also* S. REP. No. 77, 73d Cong., 1st Sess. 9-10 (1933).

⁴⁴ 401 U.S. at 632.

Each of these "bank stability" arguments is incoherent. Unless a bank is *trying* to bankrupt itself there is no reason to believe it would engage in any of these activities. A congressional attempt to ensure bank stability for the reasons articulated in *Camp* and described above is analogous to a hypothetical rule that would restrict bank loans to one per customer. This rule might be justified on the grounds that it prevents banks from suffering losses on subsequent loans in order to insure being repaid on the first loan. Such a rule would clearly do more harm than good since frequently second loans are fully justified. Banks have more than ample market incentives to restrict their lending in such a way as to maximize net revenue for the bank.

In sum, any notion that Glass-Steagall can be justified on grounds that commercial banks are somehow made safer by the Act's prohibitions is clearly misguided, since the law, if anything, accomplishes precisely the opposite result. If allowed to buy and sell stocks, commercial banks could diversify their portfolio of assets, thereby reducing risk. Similarly, by entering the investment banking business, banks could achieve cost savings in numerous ways.⁴⁵ As a firm's costs of operation are reduced, the firm necessarily becomes less risky since such a firm can earn a concomitantly lower gross return on investment without risking insolvency.

2. *Conflicts of Interest*

The Supreme Court in *Camp* articulated a separate though closely related set of congressional motives behind the Glass-Steagall Act. The legislature was said to have acted under the premise that public confidence and customer good will are essential to bank solvency.⁴⁶ Based on this premise, the Court seemed to believe that terrible things might happen if a bank depositor lost money on a

⁴⁵ For example, if allowed to buy and sell stock, banks could take better advantage of their own internal research capabilities. Commercial banks currently conduct extensive research in the normal course of their commercial lending activities. Similarly, many major banks operate extensive cash management, stock clearing, and transfer agent functions. All of these activities could be efficiently integrated into a firm's stock operations if the Glass-Steagall Act was abrogated.

⁴⁶ 401 U.S. at 631.

securities investment bought from a bank.⁴⁷ For example, the customer might withdraw his money from the bank, thereby threatening the bank's stability. Similarly, if the bank's securities department proved unprofitable, public confidence in the bank would erode.⁴⁸

None of these public confidence concerns, however, provides a persuasive justification for Glass-Steagall. There is no reason whatsoever why public confidence in a bank will be threatened more if the bank loses money in its securities operations than in its lending operations. It is even more far fetched to presume that the stability of the banking system generally is threatened by irate deposit customers making withdrawals because of losses suffered in stock purchases. Actually, the effect will be that deposits will simply flow to those banks that give sound investment advice. These banks, and *a fortiori* the banking system, will be strengthened by their securities activities. Any residual problems will be solved by deposit insurance.⁴⁹

Congress also saw a "plain conflict" between the promotional activities of stock brokers who call people up to convince them to buy stock and the more dignified "obligation of the commercial banker to render disinterested investment advice."⁵⁰ The Court quoted Senator Bulkey, a leading proponent of the Act, for the proposition that:

Obviously, the banker who has nothing to sell to his deposi-

⁴⁷ "Congress was also concerned that bank depositors might suffer losses on investments that they purchased in reliance on the relationship between the bank and its (securities) affiliate. This loss of customer good will might 'become an important handicap to a bank during a major period of security market deflation.'" 401 U.S. at 631 (citations omitted). See also 77 CONG. REC. 4028 (1933) (remarks of Rep. Fish).

⁴⁸ 401 U.S. at 631.

⁴⁹ The most obvious "residual" problem that might exist is that a commercial bank could be rendered completely insolvent by losses from its securities activities. Customers are only harmed by this to the extent that their interests are uninsured. Plainly, it is deposit insurance, rather than the prohibitions of Glass-Steagall, that insures bank stability and public confidence in banking. See M. FRIEDMAN & A. SCHWARTZ, A MONETARY HISTORY OF THE UNITED STATES, 1867-1960 (1963) (deposit insurance was the most important structural change in banking system and the change most conducive to monetary stability). See also *infra* text accompanying note 57.

⁵⁰ 401 U.S. at 633.

tors is much better qualified to advise disinterestedly and to regard diligently the safety of depositors than the banker who uses the list of depositors in his savings department to distribute circulars concerning the advantages of this, that, or the other investment on which the bank is to receive an originating profit or an underwriting profit or a distribution profit or a trading profit or any combination of such profits.⁵¹

By removing the bank's ability to profit from the sale of securities, Congress was not ensuring that banks would provide better advice than investment banks. Congress was ensuring that commercial banks would provide no advice at all.

Significantly, the Court recognized that Senator Bulkey's plans to restrict the scope of commercial banks' activities would also restrict commercial banks' profitability. In Senator Bulkey's own words, "if we want banking service to be strictly banking service, *without the expectation of additional profits* in selling something to customers, we must keep the banks out of the investment security business."⁵² The Court's reading of the legislative history in *Camp* necessarily implied an extremely broad construction of the term "security." The Court explicitly recognized that it could only interpret Glass-Steagall as representing a congressional choice that investment bank activity is "bad" and must be prohibited regardless of the effect on market efficiency: "From the perspective of competition, convenience, and expertise, there are arguments to be made in support of allowing commercial banks to enter the investment banking business. But Congress determined that the hazards outlined above made it necessary to prohibit this activity to commercial banks."⁵³

III. INTEREST GROUP THEORY

The Court's advertence to the costs Glass-Steagall would impose on commercial banks shows that the majority in *Camp* fully recognized the effect of its interpretation of Glass-Steagall. The above

⁵¹ *Id.* at 635 (quoting 75 CONG. REC. 9912 (1932)).

⁵² *Id.* at 634 (emphasis added) (quoting 75 CONG. REC. 9912 (1932)).

⁵³ *Id.* at 636.

review of the legislative history of Glass-Steagall, as summarized in *Camp*, demonstrates that the formal intentions articulated in the statute — promoting bank safety and eliminating conflicts of interest — are not advanced by enforcing the Act's mandate that commercial banks be prohibited from participating in investment banking. Moreover, the net effect of the statute, as interpreted by the Court in *Camp*, may be to thwart the Act's stated goals.⁵⁴ Thus, one is left to wonder why Glass-Steagall was enacted in the first place. Two hypotheses can be proffered. The first is that the Act is a misguided, albeit benign, attempt to accomplish its formally articulated objectives; it is a congressional mistake. The second hypothesis is that the Act can best be explained as an example of special interest group legislation. That is, Glass-Steagall represents the triumph of one special interest group, the investment bankers, over another interest group, the commercial bankers.

The first explanation, that the Act is simply a result of congressional error, is unsatisfactory for a number of reasons. First, because it is purely conclusory, it does not explain why Congress chose to completely *ban* banks from entering the field of investment banking. It seems clear that all of the hazards with which Congress was ostensibly concerned could be handled more effectively by regulation than by outright prohibition.⁵⁵ Moreover, if Congress' actual motivations were those articulated in the legislative history, why did Congress do nothing to control other equally unsound banking practices such as making unreliable commercial loans?

The Federal Deposit Insurance Corporation was also created by the Banking Act of 1933.⁵⁶ This statute requires all national banks and all state banks that are members of the Federal Reserve System to purchase federal deposit insurance. The statute made moot the issue of "public confidence" in the banking system by mitigating most depositors' risk of loss from bank failures. The effectiveness of this aspect of the insurance scheme is evidenced by the fact

⁵⁴ See *supra* text accompanying notes 32-53.

⁵⁵ For this point I am indebted to Professor Robert C. Clark, who made this observation at the 1983 session of the Harvard Law School Program of Instruction for Lawyers.

⁵⁶ 12 U.S.C. § 1811 (1982).

that runs on banks ceased.⁵⁷ It is unclear, then, why Congress did not believe it had reached its articulated goals by the imposition of deposit insurance. Equally perplexing is that Congress never explained how brokerage activities make banks riskier.

The alternative hypothesis is that Glass-Steagall was passed because a special interest group, namely investment bankers (perhaps along with some commercial bankers who wanted to leave the field), was able to persuade Congress to prohibit commercial banks from competing with the group. Interestingly, the Court's decision on standing in *Camp* supports this hypothesis. The Court held that the Investment Company Institute had standing as a competitor to challenge the decision of the Comptroller of the Currency because Congress legislated against the *competition* that the petitioners challenged.⁵⁸

Justice Harlan in dissent recognized the full import of this holding. He rejected the majority's apparent conclusion that Congress intended "to protect petitioner's class against competitive injury,"⁵⁹ and therefore dissented on standing grounds. Harlan's view was that Congress simply *could not* have intended to protect the investment community against competition from commercial bankers when it enacted Glass-Steagall. Indeed, few hints of such favor-

⁵⁷ See FRIEDMAN & SCHWARTZ, *supra* note 49, at 11; see also S. COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, THE REPORT OF THE PRESIDENT'S COMMISSION ON FINANCIAL STRUCTURE AND REGULATION 44 (1973); 1982 FEDERAL DEPOSIT INSURANCE CORPORATION ANNUAL REPORT (describing FDIC's monitoring and insurance activities); Note, *supra* note 24, at 106.

⁵⁸ 401 U.S. 621. See also *id.* at 639 (Harlan J., dissenting).

⁵⁹ *Id.* at 640 (Harlan, J., dissenting). The dissent brings into sharp focus the difference between cases such as *Railroad Co. v. Ellerman*, 105 U.S. 166 (1882), *Alabama Power Co. v. Ickes*, 302 U.S. 464 (1938), *Tennessee Power Co. v. TVA*, 306 U.S. 118 (1939), and *Perkins v. Lukens Steel Co.*, 310 U.S. 113 (1940), on the one hand, and the *Chicago Junction Case*, *Baltimore & Ohio R.R. Co. v. United States*, 264 U.S. 258 (1924), on the other. In the first group, a plaintiff who was injured on account of "lawful competition" did not have standing to "question the legality of any aspect of its competitor's operations." *Camp*, 401 U.S. at 640 (Harlan, J., dissenting) (quoting *Hardin v. Kentucky Utilities Co.*, 360 U.S. 1, 5-6 (1968)). In the *Chicago Junction Case*, the Court held that the plaintiff had standing since the statutory provision in question reflected a legislative purpose to protect a particular group against competition. *Camp*, 401 U.S. at 640-41 (Harlan, J., dissenting). Comparing the two groups of cases, the dissent rejected the proposition that Glass-Steagall was enacted to protect a particular group against competition.

itism can be gleaned from the legislative history or from the statutory language itself. Justice Harlan found it "reasonably plain that, if anything, the Act was adopted despite its anticompetitive effects rather than because of them."⁶⁰ The thrust of this approach is that it preserves a pristine, public policy oriented view of congressional motives and indirectly supports the congressional mistake hypothesis. To Harlan, since Congress had no defensible *reason* to pass legislation protecting the investment industry, it must not have done such a thing. This approach, however, has two flaws. First, it leaves us without *any* justification or explanation for the Act whatsoever. Second, Justice Harlan's approach ignores the important distinction in statutory analysis between legislative *motive* and legislative *intent*. As Judge Posner has observed:

Courts look to the language of the statute, to the legislative history and to other evidence of legislative intent, but they do not speculate on the motives of the legislators in enacting the statute. They do not, in short, conduct the kind of economic or political science inquiry that might reveal the pattern of interest group pressures behind the statute.⁶¹

Justice Harlan was correct in one respect — the ostensible intent of the Congress could not have been simply to protect a group so "unworthy" of protection as investment bankers. But what about their underlying motive — particularly in the absence of any conceivable alternative justification for their action?

A historian examining the Glass-Steagall Act would conclude that the Act was promulgated in the wake of the Depression to lend stability to the nation's faltering banking system.⁶² An economist would conclude that this legislation must be looked upon as a consumable good like any other, and, since legislative protection invariably "flows to those groups that derive the greatest value from it, regardless of overall social welfare,"⁶³ to fully understand Glass-Steagall we must look to the special interest group being

⁶⁰ 401 U.S. at 640 (Harlan, J., dissenting).

⁶¹ Posner, *supra* note 4, at 272 (footnotes omitted).

⁶² *Id.* See also Ianni, *supra* note 33, at 104.

⁶³ Posner, *supra* note 4, at 265.

particularly benefited by the statute. This analysis does not suggest that *all* legislation benefits some special interest group — only that some of it does. Other kinds of legislation, as described in an influential article by Judge Richard Posner, include (1) public interest legislation and (2) “public sentiment” legislation.⁶⁴ Public interest legislation is only enacted after an “objective weighing of demonstrable pros and cons.” Such laws generally attempt to correct market failure and thereby further the public interest by reducing such public ‘bads’ as pollution and crime or by increasing such public goods as charitable gifts.⁶⁵ Public sentiment legislation cannot be justified on any economic basis at all. Such legislation attracts wide support often at the expense of special interest groups that one might think could block such legislation. Examples of such public sentiment legislation are pornography and usury laws.⁶⁶

The Glass-Steagall Act does not fit the description of “public interest” legislation. As analyzed above, the formally articulated, public-spirited justifications for the Act are best achieved by not enforcing the statute rather than enforcing it. It is possible, however, that Glass-Steagall could be described as a peculiar kind of “public sentiment” legislation. Conceivably, Congress could have passed Glass-Steagall as a result of public pressure to “punish” the nation’s commercial banks for their role in “bringing about” the Depression. This seems an unlikely possibility. Increasing taxes would have been a more effective punishment, and besides, it is unlikely that the public would have supported a statute that raised the cost and therefore the price of commercial banking merely for the sake of doing so. It is highly unlikely that an effective political coalition could have formed around such a policy.

The triumph of a particular interest group is an especially likely

⁶⁴ *Id.* at 270-72. *But see generally* P. ARANSON, *AMERICAN GOVERNMENT: STRATEGY AND CHOICE* (1981) (arguing that *all* legislation is special interest legislation).

⁶⁵ Posner, *supra* note 4, at 271.

⁶⁶ *Id.* It is likely that many laws cannot be justified on economic grounds simply because we do not have sufficient data on the cause and effects of such legislation. For example, it may be that it is efficient to eliminate pornography because of the concomitant reduction in the crime rate or because of some other even more obscure rationale. Posner, *supra* note 4, at 271.

explanation for the passage of the Glass-Steagall Act. The theory predicts that more powerful groups are more likely to see their interests reflected in legislation than weaker groups. Commercial banks, which had been found to be largely responsible for the Depression, were in no position to adequately defend themselves during the early 1930's. The group that benefited initially from the Act were the investment bankers,⁶⁷ a small, cohesive group that was well organized and concentrated in the City of New York. It is also likely that some segment of commercial banks wanted to abandon investment banking, but only if their competitors were barred from taking customers away by offering the service. Thus the investment banks lobbying for the Act may have been aided by a small coterie of commercial bankers sympathetic to their goals. This possibility, of course, in no way detracts from the special interest group nature of the legislation. For the purposes of this article, a precise description of the interest group or coalition of such groups is not crucial. The relevant fact is that Glass-Steagall clearly represents an agreement between a special interest group and the legislature.

While the above interest group theory has immense intellectual appeal, especially when applied to a statute such as the Glass-Steagall Act where a plausible alternative justification is lacking⁶⁸ the analysis provides no guidance whatsoever to courts trying to apply laws that "have nothing to do with the public interest, whether defined in efficiency or equity terms."⁶⁹

Special interest group legislation places a heavier burden on courts than public interest or public sentiment types of legislation. The Glass-Steagall Act, as discussed below, provides an excellent example of the difficulties faced by courts when called upon to construe such legislation. When public sentiment or public interest types of legislation are construed by courts "the actual and the ostensible purposes coincide."⁷⁰ As Glass-Steagall demonstrates,

⁶⁷ See *supra* notes 54-63 and accompanying text. Cf. S. REP. NO. 77, 73d Cong., 1st Sess. 2, 3-7, 10 (1933).

⁶⁸ See Posner, *supra* note 2, at 344 (describing appeal of theory).

⁶⁹ Posner, *supra* note 4, at 266.

⁷⁰ *Id.* at 273.

when the statute represents a bargain struck between a special interest group and Congress,

it will not be clear, at least without an inquiry that is beyond the judicial competence to undertake, how completely the group prevailed upon Congress to do its will. The statute as ultimately enacted may represent a compromise with other groups; if so, the real legislative purpose may be unclear.⁷¹

IV. SETTING THE STAGE: JUDICIAL INTERPRETATION OF GLASS-STEAGALL AFTER *Camp*

The remainder of this article seeks to provide an indication of how legislation explained by the special interest group theory is likely to fare in the courts. As mentioned above, the vehicle by which this analysis will proceed is the impending Supreme Court decision in *A. G. Becker v. Board of Governors of the Federal Reserve System*. As the Court faces its commercial decision, it is clear that the Court's earlier analysis in *Camp* has crumbled under the weight of the incoherence of its statutory analysis. The Court can hardly be blamed, however, since the legislature gave it virtually nothing with which to work.

A. *The Post-Camp Period*

The Supreme Court's next opinion construing the "security" concept under Glass-Steagall came eleven years after *Camp* in *Board of Governors of the Federal Reserve System v. Investment Co. Institute* [hereinafter referred to as *Board of Governors v. ICI*].⁷² This opinion is important because it represents a sharp departure from the *Camp* decision. *Board of Governors v. ICI* set the trend for the current, permissive way that Glass-Steagall is now interpreted and brought the "closely related to banking" concept of the Bank Holding Company Act⁷³ into direct confrontation with Glass-Steagall's prohibition against banks' dealing in securities.

⁷¹ *Id.* (emphasis in original).

⁷² 450 U.S. 46 (1981).

⁷³ 12 U.S.C. § 1843(c)(8) (1982).

The Bank Holding Company Act prohibits bank holding companies from engaging in activities that are not closely related to banking. The Federal Reserve Board has been given the authority to allow bank holding companies to engage in business activities that are "so closely related to banking . . . as to be a proper incident thereto."⁷⁴ In 1972 the Federal Reserve Board amended its "Regulation Y," thereby expanding the list of permissible commercial banking activities to permit commercial bank holding companies and their affiliates to act as investment advisers to closed-end investment companies.⁷⁵ Both closed-end investment companies and open-end investment companies (which were the subject of the dispute in *Camp*⁷⁶) sell shares to customers and use the proceeds of such sales to purchase a portfolio of other securities in the open market. Banks profit from both activities in the same way, by tak-

⁷⁴ The original act provided, in part:

- (a) Except as otherwise provided in this Act, no bank holding company shall -
 - (1) after acquire direct or indirect ownership or control of any voting shares of any company which is not a bank, or . . .
 - (c) The prohibitions in this section shall not apply to . . . (6) shares of any company all the activities of which are of a financial, fiduciary, or insurance nature and which the Board after due notice and hearing, and on the basis of the record made at such hearing, by order has determined to be so closely related to the business of banking or of managing or controlling banks as to be a proper incident thereto and as to make it unnecessary for the prohibitions of this section to apply in order to carry out the purposes of this Act

Bank Holding Company Act, Pub. L. No. 84-511, § 4, 70 Stat. 133, 135-37 (1956).

The relevant exemption is now found in 12 U.S.C. § 1843(c)(8) (1982) which allows holding company ownership of:

- (8) shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto In determining whether a particular activity is a proper incident to banking or managing or controlling banks the Board shall consider whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices. In orders and regulations under this subsection, the Board may differentiate between activities commenced de novo and activities commenced by the acquisition, in whole or in part, of a going concern.

12 U.S.C. § 1843(c)(8) (1982).

⁷⁵ Board of Governors of the Fed. Reserve Sys. v. Investment Co. Inst., 450 U.S. 46, 49-50 (1981).

⁷⁶ See *supra* text accompanying notes 32-35.

ing a fee and distributing the remaining revenues among the customers on a pro rata basis. The distinction between "closed" and "open" ended funds is that an open-end investment company (also known as a mutual fund) is "continuously engaged in the issuance of its shares and stands ready at any time to redeem the securities as to which it is the issuer,"⁷⁷ while a closed-end investment company does not stand ready to redeem its shares and only issues such shares occasionally, not continuously.

Despite its earlier conclusion that serving as an investment adviser to an open-end investment company violates Glass-Steagall, in *Board of Governors v. ICI* the Supreme Court upheld a determination of the Federal Reserve Board that serving as an investment adviser to a closed-end investment company does not violate the Act. The Court opined that, for Glass-Steagall purposes, the closed-end investment company question "presents an entirely different issue" from the open-end question the Court had previously faced.⁷⁸ The Court's distinction stemmed from two factors. First, the Federal Reserve Board had expressly prohibited commercial banks from issuing, underwriting, selling, or redeeming shares of a closed-end investment company.⁷⁹ Second, closed-end investment companies were subject to "restrictions imposed by the [Federal Reserve] Board [which] . . . would also preclude the promotional pressures that are inherent in the investment banking business."⁸⁰

This opinion ignored the bank safety issues that informed *Camp* and expressly recognized that any conflict of interest problems which Congress imagined might exist when commercial banks sell securities can be solved easily by administrative regulation. This conclusion by the Court constituted a judicial amendment of the Glass-Steagall Act and an obvious departure from the previous holding in *Camp*. As *Camp* made clear, the congressional history of Glass-Steagall indicates that Congress preferred outright prohibition over regulation as the means for controlling banks' investment

⁷⁷ 450 U.S. at 51 (quoting 12 C.F.R. § 225.125(c) (1980)).

⁷⁸ *Id.* at 65-66.

⁷⁹ *Id.* at 66.

⁸⁰ *Id.* at 67.

activity.⁸¹ This conclusion was arrived at after lengthy debate.⁸² The proposition that if sufficiently regulated, a commercial bank may conduct securities activities consistent with the rationale of Glass-Steagall is completely unsupportable.

Next, the so-called dangers that the Court recognized in *Camp* are in no way diminished by the fact that the entity issuing the securities in *Board of Governors v. ICI* was a closed-end investment company while the entity in *Camp* was an open-end investment company. For example, a commercial bank is just as likely to invest its own assets in imprudent investment vehicles via one entity as via the other. Similarly, banks might make loans to customers to facilitate the purchase of closed-end investment shares just as banks might make loans to customers to facilitate purchases of shares of open-end companies. A bank is just as likely to make unsound loans to companies in which the closed-end fund has invested as it is to make unsound loans to companies in which the open-end company has invested. Finally, bank investors might suffer losses (shares in closed-end investment companies are freely traded in the secondary market) on shares in closed-end companies to the same extent as customers might suffer losses on investments in open-end companies.

For those wondering what is left of the Glass-Steagall Act after *Board of Governors v. ICI* the answer is clear. Interpretation of the Act has been taken out of the hands of the courts and placed in

⁸¹ 401 U.S. at 629-30 (citing S. REP. NO. 77, 73d Cong., 1st Sess. 10, 1933); 77 CONG. REC. 3835 (1933) (remarks of Rep. Steagall); *id.* at 4179-80 (remarks of Sen. Bulkley); 75 CONG. REC. 9913 (1932) (remarks of Sen. Bulkley) (mere existence of commercial bank securities operation "no matter how carefully and conservatively run is inconsistent with the best interests of the trust company . . . as a whole."); Perkins, *The Divorce of Commercial and Investment Banking: A History*, 88 BANKING L.J. 483, 506-07 (1971).

⁸² See *Operation of the National and Federal Reserve Banking Systems: Hearings on S. 71 Before the Subcomm. on Banking of the Senate Comm. on Banking and Currency*, 71st Cong., 3d Sess., 19-22 (1931) (testimony of J.W. Pole, Comptroller of the Currency); *id.* at 191-92 (testimony of Albert H. Wiggin, Chairman of the Board, Chase National Bank); *id.* at 238-41 (testimony of B.W. Trafford, Vice-Chairman, First National Bank of Boston); *id.* at 301-04, 318 (testimony of Charles E. Mitchell, Chairman of the Board of National City Bank of New York); *id.* at 356, 364-65 (testimony of Owen D. Young, Chairman of the Board, General Electric Co.); *id.* at 539-43 (statement of Allan M. Pope, Executive Vice-President of First National Old Colony Corp.).

the hands of the regulatory authorities. *Camp* represents an example of the judiciary implicitly enforcing the terms of a bargain struck between the legislature and a special interest group. *Board of Governors v. ICI* is an example of the Court's inability to explicitly recognize and therefore enforce the original bargain struck by the legislature. The distinction is that in the latter case a regulatory agency has persuaded the Court that enforcing the "bargain" does not achieve the Act's purported objectives. It is important to note that the regulatory agency, the Federal Reserve Board, represents the commercial banking industry, *not* the investment bankers who were the intended beneficiaries of the legislation. The Federal Reserve, as "agent" of the commercial banking interests, was easily able to convince the Court that the restrictions on bank activities imposed in *Camp* were unnecessary to bank safety. This occurred because lacking any underlying support in logic, the *Camp* decision was bound to deteriorate. As will be developed more fully below,⁸³ when the Glass-Steagall Act is involved, deference to the determination of the relevant administrative agency results in abrogation of the original legislation. The Glass-Steagall example indicates that there may be severe limitations on the efficacy of special interest group legislation, particularly on the longevity of such legislation. These limitations on the impact of special interest group legislation, at least in the case of the Glass-Steagall Act, may be far more severe than those recognized by Judge Posner.⁸⁴

B. *The Post-Modern Period: The Evisceration of Camp*

After the Securities and Exchange Commission eliminated fixed-rate brokerage commissions in 1975,⁸⁵ a group of specialty firms, called "discount" brokerage firms sprang up and began acquiring a significant share of the market for customers' securities orders.⁸⁶

⁸³ See *infra* text accompanying notes 85-111.

⁸⁴ See Posner, *supra* note 4, at 273. See also *supra* text accompanying notes 61-71.

⁸⁵ See SEC Securities Exchange Act Release No. 10383 [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,511 (Sept. 11, 1973); Securities Acts Amendments, Pub. L. No. 94-29, § 4(e)(1), 89 Stat. 104 (1975) (codified at 15 U.S.C. § 78f(e)(1) (1982)).

⁸⁶ Carrington, *Discounters Are Taking Ever-Wider Slice of Brokerage Commissions*, *SIA Study Finds*, Wall St. J., Mar. 7, 1983, at 7, col. 1.

Discount brokerage firms differ from traditional brokerage firms in that they "generally do not employ a research staff or commissioned account executives," do not give investment advice, and purchase and sell stock only when directed to do so by customers.⁸⁷

On January 7, 1983 the Federal Reserve Board authorized a commercial bank holding company, Bank America Corporation, to acquire the Charles Schwab Corporation, the sole owner of Charles Schwab and Company, the nation's largest "discount" brokerage firm.⁸⁸ The Securities Industry Association, a trade group that represents over 540 securities brokers, dealers, and investment banking companies, petitioned for judicial review of the Board's order.⁸⁹

Judge Lumbard, speaking for the Second Circuit in *Securities Industry Association v. Board of Governors of Federal Reserve System*,⁹⁰ began his opinion by acknowledging an extraordinary degree of deference to the Federal Reserve Board. The court opined that the Board's opinion, due to its expert knowledge of commercial banking, was "entitled to substantial deference"⁹¹ and must be upheld unless found to be unreasonable. In upholding the Federal Reserve Board's decision, the court analyzed Section 20 of the Glass-Steagall Act, which states that:

[N]o member bank shall be affiliated in any manner . . . with any corporation, association, business trust, or other similar organization *engaged principally in the issue, flotation, underwriting, public sale, or distribution* at wholesale or retail or through syndicate participation of stock, bonds, debentures, notes, or other securities⁹²

Since Bank of America's acquisition of Schwab made the brokerage firm an affiliate of the bank,⁹³ the bank would be in violation of

⁸⁷ Note, *A Banker's Adventures in Brokerland: Looking Through Glass-Steagall at Discount Brokerage Services*, 81 MICH. L. REV. 1498, 1498-99 (1983).

⁸⁸ *Securities Indus. Ass'n v. Board of Governors of the Fed. Reserve Sys.*, 716 F.2d 92, 94 (2d Cir. 1983).

⁸⁹ *Id.* at 94.

⁹⁰ 716 F.2d 92.

⁹¹ *Id.* at 95.

⁹² *Id.* at 95-96 (quoting 12 U.S.C. § 377 (1976)) (emphasis by the court).

⁹³ 716 F.2d at 96 (citing 12 U.S.C. § 221(a)(b) (1976)).

Section 20 if Schwab were “engaged principally in the . . . public sale or distribution of . . . stocks, bonds, debentures, notes or other securities.”⁹⁴ Despite the fact that Schwab’s business practices, which include mass advertising via national television, seem to plainly involve the public sale of stock, the Second Circuit held that the mere execution of orders for the purchase and sale of securities on behalf of others does not involve the “public sale” of securities.⁹⁵

Turning to the policies behind the Glass-Steagall Act, the court made a persuasive argument in support of its conclusion. Consistent with the methodology of *Board of Governors v. ICI*, Judge Lumbard addressed the two ostensible concerns of the legislature and concluded that neither of these concerns was threatened by commercial bank involvement in the discount brokerage business. First, the court examined the bank safety concern.⁹⁶ As discussed earlier, the principal safety concern is that the bank might invest its own assets in imprudent stock or securities investments.⁹⁷ The court concluded that since Schwab trades only as agent, it would not be possible for Bank of America to invest its own assets in any unwise investment contract.⁹⁸ Moreover, because Schwab does not offer investment advice to customers, the court considered that “the losses that some customers will sustain on trades executed through Schwab will be unlikely to impair public confidence in the Bank.”⁹⁹ The court then turned to the second legislative goal—that bankers conduct themselves in such a way that there is no appearance of conflict between their primary obligation to give disinterested investment advice and their promotional role as an investment banker. This goal is not threatened according to the court because Schwab has no “‘salesman’s interest’ in the securities it trades”¹⁰⁰ and, therefore, the Bank has no incentive to promote

⁹⁴ See *supra* text accompanying note 92.

⁹⁵ 716 F.2d at 96.

⁹⁶ See *supra* text accompanying notes 38-45.

⁹⁷ *Id.*

⁹⁸ 716 F.2d at 97, 98.

⁹⁹ *Id.* at 98.

¹⁰⁰ *Id.*

one security over another.¹⁰¹ Schwab's stated policy of not offering any investment advice also strongly supported this conclusion.

The court next considered whether Schwab's discount brokerage business was in violation of The Bank Holding Company Act.¹⁰² As discussed above,¹⁰³ the relevant inquiry here is whether the discount brokerage services offered by Schwab were "so closely related to banking . . . as to be a proper incident thereto."¹⁰⁴ Here, exclusively on the strength of its decision to afford great deference to the Federal Reserve Board, the court upheld the Board's conclusion that the brokerage business is closely related to banking.¹⁰⁵ Under this analysis, however, the Bank Holding Company Act would completely swallow the Glass-Steagall Act. Giving investment advice is closely related to banking,¹⁰⁶ buying and selling stock is closely related to banking,¹⁰⁷ and underwriting and trading securities are presumably closely related to banking.¹⁰⁸

The court analyzed commercial bank involvement in the discount brokerage business on the basis of whether this activity actually posed risks to the nation's banking system. The answer, of course, was a resounding "no." And, in fact, the division between commercial and investment banking has eroded even further.

Subsequent to the Second Circuit's opinion in *Securities Industry Association v. Board of Governors*, the Comptroller of the Currency approved an application by the American National Bank, which had previously obtained permission to operate a discount brokerage business, to establish an operating subsidiary to provide an investment advisory service.¹⁰⁹ The combination of these two

¹⁰¹ *Id.*

¹⁰² *Id.* at 100 (construing 12 U.S.C. §§ 1841 *et seq.* (1976)).

¹⁰³ See *supra* text accompanying note 74.

¹⁰⁴ 12 U.S.C. § 1843(c)(8) (1982).

¹⁰⁵ 716 F.2d at 102.

¹⁰⁶ 450 U.S. 46, 55 (1981).

¹⁰⁷ 716 F.2d 101.

¹⁰⁸ Banks traditionally underwrite municipal bonds and participate in investment banking abroad. Trading activity is widely conducted by commercial banks not only in municipal bonds, but also in the foreign exchange and government securities markets.

¹⁰⁹ *Ruling Allows Bank to Offer Investment Advisory Service*, *American Banker*, Jan. 14, 1983, § 1, at 4.

events — the Second Circuit decision to permit commercial banks to engage in discount brokerage, and the decision of the Comptroller to allow such banks to provide investment advice — abrogates the “bargain” between the special interest group and Congress and leaves very little of Glass-Steagall intact. The nucleus of facts relied upon to support the court’s decision in *Securities Industry Association v. Board of Governors* is dramatically different when a bank is also operating an investment advisory service in its constellation of financial services. The Comptroller’s ruling obviously contradicts the court’s finding that, because Schwab did not “offer investment advice, customers who trade unsuccessfully will have only themselves, and not Schwab or the Bank, to blame for their mistakes.”¹¹⁰ Other potential hazards such as the danger that banks might make loans to customers to facilitate the purchase of securities promoted by the bank, or that public confidence in the bank would be impaired if stocks recommended by the bank fared poorly, are also implicated by the combination of these two decisions. American National Bank’s discount brokerage firm and investment adviser share the same name (Impact) and address (the headquarters location of the bank). Furthermore, the bank’s application indicated that “there may be some referrals of customer/clients from brokers to adviser and vice-versa.”¹¹¹

As a result of the Comptroller’s decision, the rockslide that began with *Board of Governors v. ICI* is now an avalanche. As the commercial paper litigation illustrates, the trend noted above — administrative intrusion into the bargain struck between an interest group and the legislature — is now the norm in Glass-Steagall litigation.

C. *The Commercial Paper Case*

The Comptroller’s favorable decision in the application of the American National Bank left only one major aspect of Glass-Steagall unscathed. This aspect — commercial bank acquisition of securities as principal — is an important facet of the dispute in *A.G.*

¹¹⁰ 716 F.2d at 98.

¹¹¹ American Banker, *supra* note 109, at 4.

Becker v. Board of Governors.¹¹² This case represents another example of judicial reliance on the expertise of an administrative agency. Judge Wilkie, speaking for a divided panel of the Court of Appeals for the District of Columbia determined that:

The task of the reviewing court is not to interpret the statute as it [thinks] best but rather the narrower inquiry into whether the [agency's] construction was 'sufficiently reasonable' to be accepted by a reviewing court To satisfy this standard it is not necessary for a court to find that the agency's construction was the only reasonable one or even the reading the court would have reached if the question initially had arisen in a judicial proceeding.¹¹³

The court advanced four reasons why the Federal Reserve Board's opinion was entitled to such deference.¹¹⁴ First, the Board's general supervisory powers over member banks convinced the majority that Congress had delegated to the Board primary and substantial responsibility for administering federal regulation of the national banking system.¹¹⁵ Second, because the banking system is highly technical and specialized, the Board's judgment should be conclusive on any close question since their "specialized experience gives them an advantage judges cannot possibly have" when ascertaining congressional intent.¹¹⁶ Third, the court concluded that deference to the Board's conclusion was appropriate because "the agency's decision applied general, undefined statutory terms — notes and securities — to particular facts."¹¹⁷ Fourth, the

¹¹² 693 F.2d 136, 140-41 (D.C. Cir. 1982), *cert. granted sub nom. Securities Indus. Ass'n v. Board of Governors*, 104 S. Ct. 65 (1983). *Becker* arose from the following events. On July 26, 1978, Bankers Trust Company began selling third party commercial paper. See Note, *supra* note 24, at 115. On September 26, 1980, the Federal Reserve Board ruled that Bankers Trust's participation in the commercial paper market did not violate Glass-Steagall. Federal Reserve System, Statement Regarding Petitions to Initiate Enforcement Action (Sept. 26, 1980) (unpublished).

¹¹³ 693 F.2d 136, 140 (citations omitted).

¹¹⁴ The court nowhere seems to realize that the Federal Reserve Board's analysis, as that of an agent for the commercial banks, may not be totally disinterested.

¹¹⁵ *Id.* at 140. See also 12 U.S.C. § 248 (1976).

¹¹⁶ *Id.* (quoting *Board of Governors of the Federal Reserve Sys. v. Agnew*, 329 U.S. 441 (1947)).

¹¹⁷ *Id.*

sheer thoroughness of the Board's consideration of the problem indicated to the court that great deference was justified.¹¹⁸

The court next made an independent inquiry into the language and legislative history. However, the majority, unlike the majority in *Camp*, failed to recognize the protectionist nature of the legislation it was called upon to interpret, and therefore, inevitably reached a different result. Judge Wilkie considered whether "commercial paper" more closely resembles a note evidencing a bank loan (which is of course permitted under the Act) or an investment note (which commercial banks are prohibited from underwriting).¹¹⁹ As noted earlier,¹²⁰ this sort of inquiry is bound to be unfruitful because the dichotomy between investment banking and commercial banking is more apparent than real. In the end the D.C. Circuit acknowledged this, finding the statutory language "not conclusive."

The D.C. Circuit made an accurate assessment of the ostensible legislative intent as articulated in *Camp*. The court concluded that "bank stability" was not threatened by commercial paper sales and any "conflict of interest presented here may be entirely eliminated by an authorized regulation of the Board."¹²¹ But by failing to recognize that it was construing a piece of special interest group legislation, the court reached a perfectly logical result that was completely at odds with the protectionist origins of the Act. The court correctly observed that commercial paper is very safe, as evidenced by its low default rate and short maturity.¹²² The court also pointed out — again correctly — that commercial paper is only purchased by large and sophisticated investors such as "pension funds, money market funds, insurance companies and nonfinancial corporations with large amounts of idle cash."¹²³ The court concluded the bank's purchase of commercial paper was "less risky

¹¹⁸ *Id.* at 141.

¹¹⁹ *Id.* at 144.

¹²⁰ See *supra* text accompanying notes 24-31.

¹²¹ *Becker*, 693 F.2d at 151 n.96.

¹²² *Id.* at 149.

¹²³ *Id.* See also Hurley, *The Commercial Paper Market*, 63 FED. RES. BULL. 525 (1977); Comment, *The Commercial Paper Market and The Securities Act*, 39 U. CHI. L. REV. 362 (1972).

even than banks' ordinary commercial lending."¹²⁴

Given that all of this is true, this analysis applies with equal force to a bank's sale of large blocks of blue chip stock to institutional investors — an activity clearly prohibited by the plain language of Glass-Steagall. Moreover, the lack of generality in the court's argument is seen when one realizes that the court's rationale would evaporate if applied to the sale of commercial paper in smaller denominations to the general public.¹²⁵ This problem was finessed by the D.C. Circuit by turning to the universal bromide — deference to the appropriate administrative agency, the Federal Reserve Board. The Board "will be called upon to determine in varying fact situations the scope of activities that Congress intended to permit banks to undertake."¹²⁶ The majority in *A.G. Becker v. Board of Governors* did not enforce the bargain struck between the legislature and the special interest group proponents of the legislation. Distinguishing between motive and intent, it is obvious that bank stability was only the purported *intent* of the Act. The actual *motive* consisted of protecting a special interest group — investment bankers. There is ample evidence that this group will be seriously injured by the court's decision because their market share of the commercial paper industry faces serious erosion as other banks enter the fray.¹²⁷

In reaching its decision, the D.C. Circuit also independently examined the legislative history of Glass-Steagall to determine whether Congress considered commercial paper to be included within the scope of Glass-Steagall.¹²⁸ Although this inquiry is irrelevant to the policies that Glass-Steagall is supposed to advance, such an inquiry might have led the court to enforce the bargain

¹²⁴ 693 F.2d at 149.

¹²⁵ *See id.* at 151-52.

¹²⁶ *Id.*

¹²⁷ 693 F.2d at 138 (other banks await outcome of legal proceedings before entering market); Bennet, *Corporate Loans Soar at Banks*, N.Y. Times, Dec. 16, 1980, § D (Business), at 1; SECURITIES WEEK, Dec. 18, 1978, at 2.

¹²⁸ 693 F.2d at 144-45. Note that there have been dramatic changes in the commercial paper market since Glass-Steagall was enacted. In the 1930s, when the Act was passed, commercial paper was not promoted or traded the way it is today. Commercial paper was simply purchased by banks and held to maturity as an asset. Note, *supra* note 24, at 117-18.

struck when the Act was passed. In this case it did not because the court did not distinguish between motive and intent.

The court also analyzed the policies behind the Act and concluded that commercial bank underwriting does not pose the conflicts of interest envisioned by the drafters of Glass-Steagall. The court first observed that, as a practical matter, a bank could not use its credit facilities to facilitate the sale of its commercial paper because the interest on such credit is higher than the interest on the commercial paper. In like fashion the court was not concerned that a bank might suffer a loss of public confidence or depositor good will by promoting commercial paper.¹²⁹ As the court noted, commercial paper is purchased only by investors capable of fending for themselves, and the debt instruments are issued only by corporations about whom current financial data is widely available.¹³⁰ The court was certainly correct that commercial bank trading of commercial paper involves none of the conflicts of interest that worried Congress. The Circuit Court failed to observe, however, that none of the other activities proscribed by Glass-Steagall pose such dangers either, especially when coupled with strict regulatory supervision.¹³¹

It is readily apparent that courts dealing with the Act on a case by case basis have consistently failed to enforce the deal struck between the special interest group and the legislature. Courts have no capacity to enforce the statute as a "bargain." The judiciary was not a party to the original deal struck in Congress and thus was not privy to the true motives informing the Act. Moreover, the parties whose interests are damaged by the Act have every incentive to litigate and proffer interpretations contrary to the original motives. The cases demonstrate that these parties have been able to destroy the theoretical justifications of the Act, thereby leaving the courts with no alternative but to reach results that undermine the Act. This is an inevitable result of the mechanics of the judicial

¹²⁹ 693 F.2d at 150.

¹³⁰ *Id.* at 150-51 ("even if a commercial paper issuer were to default, the sophisticated purchasers of commercial paper will understand that this paper is not backed by the guarantees on commercial bank deposits").

¹³¹ *Id.* at 151.

process itself.¹³² Judges must write opinions. These opinions must be persuasive, and to be persuasive they must be logical. Special interest legislation, such as Glass-Steagall, passed in order to favor a special interest group cannot achieve this purpose unless courts are given some basis in logic to enforce it. No such logical underpinnings accompanied Glass-Steagall, and the Act has been eviscerated.

Glass-Steagall does not actually promote bank safety, despite the fact that this is the primary ostensible legislative purpose. Furthermore, whatever conflicts of interest may arise from bank involvement in securities activity, they can be ameliorated adequately by regulation. Judicial recognition of these facts, coupled with deference to administrative expertise by an agency that represents interests opposed to the prohibitions of the Act has resulted in a telling defeat for a major piece of special interest group legislation. This defeat indicates the inherent difficulty of enforcing this kind of legislation generally and leads to the inevitable conclusion that under some circumstances special interest group legislation is more costly and less resilient than either public interest or public sentiment kinds of statutes.¹³³

V. JUDICIAL BEHAVIOR WHEN CONFRONTED WITH SPECIAL INTEREST GROUP LEGISLATION

In *Camp* the Supreme Court expressed recognition of the underlying protectionist nature of the Glass-Steagall Act. The Court's decision made little sense, but was perfectly consistent with the congressional motives behind the Act. In *Board of Governors v. ICI*, however, the Court completely ignored the motivating factors that resulted in the Glass-Steagall Act being passed. The Court instead examined only Congress' stated intent.

The stated intentions behind Glass-Steagall are impossible to apply coherently. Bank safety and the elimination of conflicts of interest are the articulated goals but application of the statutory

¹³² See generally B. CARDOZO, *THE NATURE OF THE JUDICIAL PROCESS* (1949).

¹³³ A different case is presented when the regulatory agency is policing and enforcing the legislation for the benefit of the special interest group.

language does not achieve these ends and to some extent the statutory language is actually at odds with the legislative intent. Strict judicial application of the statutory language by the courts would reach results consistent with the terms of the bargain described in this article.

However, in construing the Glass-Steagall Act, courts have sometimes given implicit recognition to the congressional motives and at other times have given explicit recognition to ostensible congressional intent.¹³⁴

Courts have also relied extensively on the expertise of administrative agencies in construing Glass-Steagall. These agencies have no particular authority or power to administer the Glass-Steagall Act — their power is only of a “general supervisory” nature.¹³⁵ Yet courts have permitted the advice of these agencies which represent interests hostile to the Act, effectively to undermine a long-standing legislative bargain. Finally courts have never settled on whether to construe the Glass-Steagall Act narrowly or broadly. This is surprising in one sense. The statute is, after all, more than fifty years old. In another sense this unsettled state of affairs is entirely understandable. It can be attributed to the incongruence between the stated intent and the actual motive behind the statute — it is *impossible* to apply the statute consistently without recognition of the true motive of the legislature.

A. *The Role of Legislative Intent in Reviewing Special Interest Group Legislation*

A statute passed at the behest of a special interest group is as legitimate as either of the other kinds of statutes (public interest and public sentiment) described above.¹³⁶ All three sorts of statutes are the normal and predictable outcomes of the legislative process. Often statutes will be difficult, if not impossible to catego-

¹³⁴ See *supra* text accompanying notes 32-53 (discussion of *ICI v. Camp*).

¹³⁵ 12 U.S.C. § 248 (1976).

¹³⁶ The Glass-Steagall Act is perhaps an extreme example of special interest group legislation.

size.¹³⁷ As Judge Posner has observed, courts do not have "the research tools that they would need to discover the motives behind the legislation."¹³⁸ Once we recognize the possibility that the other types of statutes exist, we must recognize the possibility of judicial error in the categorization process. This element must be weighed heavily before affording different judicial treatment for special interest group legislation.

Furthermore, once legislators have struck political bargains with a special interest group, both sides often have strong incentives to cover their tracks by obfuscating their true purposes. Thus, even if legislators had the resources to "conduct the kind of economic or political science inquiry that might reveal the pattern of interest group pressures behind the statute," it is unlikely that they would find the results sufficiently conclusive to be of value.¹³⁹ Judges must limit the scope of their judicial inquiry to the formal public legislative and statutory record. It is also true, on the other hand, that some, if not all, of the obfuscation that takes place following a political bargain between an interest group and a legislature will be reflected in the legislative history of the Act. Posner, however, believes it to be more realistic to assume that the legislative history reflects "the deal struck by the sponsors of the bill."¹⁴⁰ In the case of the Glass-Steagall Act, however, and undoubtedly other laws as well, the terms of the bargain are not accurately reflected in such documents as committee reports and remarks to the congressional record.¹⁴¹ Only the plain language of the statute serves as trustworthy embodiment of the bargain flowing from a special interest statute. Posner argues that post-enactment expressions of legislative intent are worthy of "little or no weight"¹⁴² since the deal is over once the statute is enacted and such subsequent expressions might simply express the desire of one or two particular legislators to renege on the deal. Posner, however, suggests no reason for his con-

¹³⁷ See Posner, *supra* note 4, at 272 (boundary between special interest group legislation and public interest group legislation is indistinct).

¹³⁸ *Id.*

¹³⁹ *Id.*

¹⁴⁰ *Id.* at 275.

¹⁴¹ *But see* Posner, *supra* note 4, at 274-75.

¹⁴² *Id.* at 275.

clusion that pre-enactment history is somehow entitled to more weight. While the legislature *as a whole* can renege on a deal, one or two individual legislators cannot. Legislative history, whether it is created before or after a statute is enacted, is likely to be purposefully deceptive or to be an effort by a small number of congressmen to renege on their bargain.

B. *The Role of Deference to Administrative Authority in Reviewing Special Interest Group Legislation*

At least in the case of the Glass-Steagall Act, deference to administrative authority may lead to the invalidation of legislation that has been motivated by special interest groups. One need not embrace a "capture" theory of administrative rulemaking to see why this is so.¹⁴³ It is noteworthy that in evaluating the legality of commercial bank sales of commercial paper, the Federal Reserve Board followed the same line of reasoning as the court in *A.G. Becker v. Board of Governors*.¹⁴⁴ First the Board, examining what it described as "indirect" historical evidence, concluded that Congress did not consider commercial paper to be a security when it passed the Act.¹⁴⁵ In reaching this conclusion, the Board also emphasized that a commercial bank's sales of commercial paper does not threaten the policies behind Glass-Steagall because the Board's own regulatory expertise would sufficiently protect the public from any unsound banking practices that might result when commercial banks sell commercial paper.¹⁴⁶ Although such analysis is plausibly correct, it ignores the true motives behind Congress' decision to divide commercial and investment banking, and substitutes the will of an administrative agency for the agreement struck with the legislature.

¹⁴³ As used here, "capture theory" represents the idea that frequently regulatory agencies come to be dominated by the industries regulated. Posner, *supra* note 2, at 341. See also S. HUNTINGTON, *The Marasmus of the ICC: The Commission, the Railroads, and the Public Interest in Public Administration and Policy*, in *SELECTED ESSAYS* (P. Wolled ed. 1966); H. ZIEGLER, *INTEREST GROUPS IN AMERICAN SOCIETY* 93-126 (1964).

¹⁴⁴ See *supra* text accompanying notes 112-131.

¹⁴⁵ Federal Reserve Statement, *supra* note 112, at 14. See also Note, *supra* note 24, at 116.

¹⁴⁶ See Federal Reserve Statement, *supra* note 112, at 25.

Judicial deference to the administrative decision-making process also may result in a dramatic increase in the costs to an interest group of getting what it wants from a legislature. If the interest group must not only persuade Congress (and such persuasion is highly costly) to pass a set of rules, but also must persuade an administrative agency to enforce the rules, the costs increase dramatically. The price of getting a statute passed represents a one-time fixed expense. The cost of continuing influence with an administrative agency is ongoing. In the Glass-Steagall example used in this article, the costs to commercial banks of influencing administrative outcomes regarding Glass-Steagall decisions can be amortized over dozens of other issues that banks are constantly debating with their regulators. Commercial banks can bargain with the regulators who have incentives to maximize both their own and their clients' influence vis-a-vis other interests, and can give up ground in other areas in order to achieve the desired result regarding Glass-Steagall. Investment banks are regulated by the Securities Exchange Commission, and have little if any contact with the Federal Reserve Board, or the Comptroller, who regulate banks.¹⁴⁷ These investment banks — the intended beneficiaries of the statute — have nothing to bargain with when dealing with agencies.

At first glance, therefore, one's view of the proper degree of deference to administrative authority when reviewing special interest group legislation depends largely on how one views the particular legislation in the first place. If the increased cost of administrative deference actually cuts down on the amount of such legislation, then those generally opposed to this kind of legislation will favor administrative agency involvement. It is more likely, however, that

¹⁴⁷ Commercial banks must be chartered under either state or federal law. Federally chartered ("national") banks are regulated by the Comptroller of the Currency, 12 U.S.C. §§ 21-24, 26-27 (1976 & Supp. v. 1981). National banks must also join the Federal Reserve System, 12 U.S.C. § 222 (1976). State chartered ("State") banks are regulated by the Federal Reserve Board ("Fed") if they join the Federal Reserve System, 12 U.S.C. §§ 321, 324-25 (1976). Thus either the Comptroller or the Fed will have primary regulatory authority over national banks or state banks.

Banks are subject to the supervision of the Federal Deposit Insurance Corporation (FDIC) if they are federally insured. National banks are required to carry such insurance. 12 U.S.C. § 222, 1814(b) (1976). The vast majority of state banks voluntarily purchase such insurance. 1980 FDIC ANN. REP. 226.

fear of judicial deference to administrative agencies will result in a proliferation of legislation that allows interest group members to achieve enforcement by circumventing administrative bodies.¹⁴⁸ Creating express private rights of action is the most satisfactory way to achieve this result. This is consistent with the court's decision on the standing question in *Camp*.¹⁴⁹ Of course, in the case of the Glass-Steagall Act, there was no way for either side to predict the degree of deference that is being awarded administrative agencies, since Glass-Steagall was passed in 1933, while the Administrative Procedures Act did not become law until 1946. As for statutes passed more recently, however, the precise standard of administrative review, like the presence of a private right of action, is simply part of the deal that was struck with the interest group, and courts should not intervene in this process.

C. *Statutory Construction*

Courts thwart the deals struck between special interest groups and legislatures in numerous ways as a purely natural consequence of the judicial function. When courts invalidate legislation because it is not "rationally related to a proper legislative purpose," laws are often being invalidated merely because they are procured by some interest group.¹⁵⁰ Similarly, the long-held rule that statutes in derogation of the common law be strictly construed seems designed to thwart special interest legislation.¹⁵¹ Recognition of the fact of special interest group legislation implies that these judicially created doctrines should be abandoned by courts, since they intrude upon the bargaining process that is a hallmark of our legislative system. Recognition of the place of legislation that affords

¹⁴⁸ It is also likely that interest groups will attempt to convince Congress that there is a strong need for administrative supervision over the activities of their competitors. Such supervision will, of course, impose additional costs on the operations of these competitors, and thereby serve the interests of the competitors not faced with such costs.

¹⁴⁹ See *supra* text accompanying notes 58-61.

¹⁵⁰ See generally R. POSNER, *ECONOMIC ANALYSIS OF LAW* 495-96 (2d ed. 1977); Linde, *Due Process of Lawmaking*, 55 NEB. L. REV. 197 (1976); Posner, *supra* note 4, at 285; but see Michelman, *Politics and Values or What's Really Wrong With Rationality Review*, 13 CREIGHTON L. REV. 487, 503-06 (1979).

¹⁵¹ Cf. G. CALABRESI, *A COMMON LAW FOR THE AGE OF STATUTES* 4, 15-25, 132-37, 155-57 (1982) (discussing the rule).

special protection to certain factions has a long and distinguished place in political science literature.¹⁵² As Holmes once said: "It is no sufficient condemnation of legislation that it favors one class at the expense of another; for much or all legislation does that."¹⁵³ It is beyond peradventure, therefore, that it is improper for courts to disfavor legislation merely because it is the product of a bargain struck with a special interest group. Thus, the Supreme Court is faced with a dilemma in *Becker*. On the one hand, it can promote more efficient markets by allowing banks to deal in commercial paper but only by failing to enforce a clearly constitutional, legitimate statute. But preserving the "bargain" will not further the ostensible intent of Congress in preserving a well-functioning financial market.

The purpose of this paper has been to point out that, by its very structure, an independent judiciary places severe obstacles on the efficacy and longevity of special interest legislation. This independent judiciary is not a beneficiary of the bargain between the legislature and the interest group and thus has no incentive to enforce the bargain unless it is apparent in the words of the statute. Moreover, the judiciary must justify its decisions, but special interest legislation such as Glass-Steagall simply cannot be justified absent recognition of the bargain the parties have attempted to obfuscate.

¹⁵² See, e.g., THE FEDERALIST No. 10 (J. Madison); O.W. HOLMES, *Herbert Spencer: Legislation and Empiricism*, in JUSTICE OLIVER WENDALL HOLMES: HIS BOOK NOTICES AND UNCOLLECTED LETTERS AND PAPERS, 104, 107-09 (H. Shriver ed. 1936) ("the more powerful interests must be more or less reflected in legislation"); D. TRUMAN, *THE GOVERNMENTAL PROCESS* (1951); Gunther, *The Supreme Court, 1971 Term-Foreward: In Search of Evolving Doctrine on a Changing Court: A Model for a New Equal Protection*, 86 HARV. L. REV. 1, 20-21, 23 (1972).

¹⁵³ O.W. HOLMES, *supra* note 152, at 108.