Big banks exist to game the system, say critics

Finance guru Ed Kane and blogger James Kwak have done a terrific tag-team take down on the argument in favor of big banks.

But I'll save you the trouble of wading through it: Essentially, Kane and Kwak say that the downside for shareholders of the bloated, inefficient bureaucracies that characterize Citigroup and to a progressively lesser extent Bank of America, Wells Fargo, and JP Morgan Chase is outweighed by their ability to lean on taxpayers for support.

Come again? To boil it all down: The rationale for size is that the complexity that it produces, thanks to financial engineering, lets banks capture their regulators. So too big to fail is the very essence of the big bank model.

Money quote: "The point of structured finance is not just to reduce capital requirements, but to make it harder for regulators to estimate systemic risk implications and easier for them to ignore what is going on."

How's that for a good reason to let them get as big as they want?

I also see that the House Financial Services Committee voted yesterday to give regulators the ability to break up such banks. That's a step in the right direction. But the bill would be better if it required them to do that.

Again, regulators already have the power to regulate. It's the willingness to regulate that's been missing, simply because big banks have captured them. That's why folks like Steve Waldman say the solution requires changing the structure of the financial system, not writing specific rules involving capital, leverage and the like. A smart bank lawyer can always find a way around those.

To borrow Kwak's phrasing, the bigger and fatter the mouse, the more easily it can escape the cat. Weird analogy, I know. But financial crises tend to defy standard description.