The Auto Bailout and the Rule of Law

Todd Zywicki

When President Dwight Eisenhower named Charles Wilson — then the president of General Motors — to be his secretary of defense in 1953, some senators considering the nomination wondered whether Wilson could distinguish his loyalty to GM from his obligations to the country. Wilson assured them that he could, but then added that he did not think a conflict would ever come up. “For years I have thought that what was good for the country was good for General Motors, and vice versa,” he said in his confirmation hearing.

Wilson’s statement — especially that “vice versa” — was long considered the epitome of corporatist excess. To many, it represented the view that the government existed to advance the interests of large corporations (and, of course, vice versa), even if the arrangement came at the expense of average citizens and workers.

In the past three years, however, Wilson’s attitude has come back into vogue, as a new approach to the relationship between the government and the private sector has taken hold in Washington. That approach — a kind of state capitalism that seeks to entangle the government and large corporations in order to allow for careful management of the economy — is perhaps best embodied in the government bailout and subsequent bankruptcy of Wilson’s old company, and of one of its longstanding competitors.

The bailouts of General Motors and Chrysler have been held up by President Obama and his supporters as a great success story — proof that, by working together, government and business can save jobs and strengthen the economy. But this popular narrative is dangerously misleading. Far from a success story, the events surrounding the bailouts

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offer a cautionary tale of executive overreach. And their example clarifies the Obama administration’s broader approach to economic policy—an approach that is both harmful to economic growth and dangerous to the rule of law.

**THE FAIRY TALE**

By December 2008, years of decline had finally caught up with Chrysler and General Motors. Unlike Ford, which had moved aggressively to fix its longstanding problems—chiefly by shedding unprofitable subsidiaries and renegotiating labor agreements—GM and Chrysler were still plagued by incompetence and inefficiency.

Both automakers were burdened with labor contracts that undermined their flexibility and saddled them with massive retiree pension and health-benefit costs. For years, both companies had also been losing market share: Once-proud GM had lost $40 billion in 2007, and in 2008 alone saw its sales decline by 45%. Chrysler, meanwhile, was languishing under the inept management of Cerberus Capital, which had bought the company in the spring of 2007 from the German automaker Daimler. (Daimler had merged with Chrysler in 1998 only to see its new American acquisition become an unsustainable liability.) By 2008, Chrysler’s market share had been declining precipitously for a decade, falling by more than 30% in that year alone.

Finally, the onset of the credit crunch and financial crisis in the fall of 2008 proved to be the companies’ death knell. But though their fates seemed to be sealed, both automakers brazenly refused to make plans for bankruptcy filings. They assumed that the federal government would not allow them to suffer the same fate as most other poorly managed companies in America. So they pleaded for a federal bailout, arguing that Washington’s failure to provide one would result in the companies’ liquidation—in part precisely because the automakers’ failure to prepare for bankruptcy filings would end up producing “disorderly” bankruptcies that, in turn, would make it difficult to keep the companies alive. And liquidation, they argued, would eliminate thousands of jobs at the companies themselves, not to mention thousands more at suppliers and dealers. It would also destroy the companies’ underfunded retiree pension and health benefits and—because they were backed by the Pension Benefit Guaranty Corporation, a government agency that guarantees some private pension systems—might in turn foist those
obligations on the taxpayer. With the economy already reeling from the financial crisis, the automakers insisted, the shock of massive auto-industry layoffs would be too much to take.

On December 11, 2008, the House of Representatives buckled under the automakers’ demands, voting (largely along party lines) in favor of a $14 billion bailout. The next day, however, the Senate voted down the legislation. A week later, lame-duck President George W. Bush and Treasury Secretary Henry Paulson intervened. Announcing that the administration would offer the automakers loans with terms similar to the ones Congress had voted down, Bush gave GM and Chrysler three months to develop restructuring plans and prove they could become viable companies. To help the automakers through that phase (and a possible Chapter 11 bankruptcy), the administration extended them $17.4 billion from the Troubled Asset Relief Program, which had originally been set up to buy assets and equities from the financial sector in the wake of the mortgage crisis.

In March 2009, when the lifeline extended by the Bush administration had run out, President Obama stepped in. The administration forced out the CEO of General Motors, Rick Wagoner, and gave Chrysler 30 days to finalize a merger with the Italian automaker Fiat. In exchange, the companies received another (and even larger) round of government loans. In the end, almost $77 billion in TARP funds was diverted to GM and Chrysler.

But in spite of the generous loans, extensions, and second chances, the Obama administration finally concluded that the companies’ restructuring plans were insufficient. In the spring of 2009, it directed both automakers to proceed into Chapter 11 bankruptcy—Chrysler filed on April 30, and GM on June 1. In both cases, bankruptcy involved creating new companies—the so-called “new Chrysler” and “new GM”—in which the federal government would have a significant stake, and to which the bulk of the assets of the original companies (including all of their plants, equipment, brands, and trademarks) would be sold. The original companies, meanwhile, would settle their obligations to creditors and shed those assets that would not be transferred to the new companies. Their shareholders would be all but wiped out.

The automakers’ house-cleaning didn’t take long; within two months of filing, each company had emerged from its bankruptcy. By the summer of 2009, the new General Motors was a somewhat smaller and leaner
company, having shed about a third of its American work force. It was owned jointly by the federal government (which held 60% of the stock), the United Auto Workers union (with 17%), and the Canadian government (with 12% ownership). Chrysler, meanwhile, emerged through an alliance with Fiat, under which the new company was owned by the United Auto Workers (with a 55% share), Fiat (with 20%), the United States government (with 8%), and Canada (with 2%). (Both GM and Chrysler have significant operations and large work forces in Canada; the Canadian government, facing pressures similar to those exerted on lawmakers in the U.S., also contributed bailout funds—about $800 million for Chrysler and $2.4 billion for GM—hence its ownership stakes.)

The idea was for the companies to go public within a few months, at which point the U.S. government would sell most of its shares. GM did in fact go public in November 2010, raising about $20 billion in the biggest initial public offering in American history. Through the stock sale, the government’s share in the company was reduced to about 30%. The new Chrysler has not yet gone public—indeed, the company reported a $200 million loss in the last quarter of 2010—but industry analysts believe it will later this year.

To the Obama administration, and to many other champions of the auto bailout in Congress and the press, the story outlined here is one of extraordinary success. “Supporting the American auto industry required tough decisions and shared sacrifices, but it helped save jobs, rescue an industry at the heart of America’s manufacturing sector, and make it more competitive for the future,” President Obama said when the new General Motors went public last November. Then-speaker of the House Nancy Pelosi echoed his view, arguing: “In the midst of a severe recession, congressional Democrats and President Obama took difficult emergency action to rescue American auto companies and strengthen critical pillars of our manufacturing sector, while protecting taxpayers.”

Of course, this “success narrative” is based on a particular reading of the events surrounding the bailout. According to that reading, the nature of the ’08 financial crisis—as well as the economic importance of the auto industry—meant that the government simply could not let GM and Chrysler go under. But at least the unprecedented cooperation between the government and the automakers was undertaken in a deliberate, careful way—using the government’s special authority to contend with the economic crisis in order to guide the companies through an orderly...
re-organization (rather than the dreaded chaotic collapse). As a result, the companies were saved, and now they have a chance to thrive again.

Unfortunately, every part of this reading of events is wrong.

THE BAILOUT

The first premise of the “success story” narrative is that, if not for the bailout, General Motors and Chrysler would have been liquidated—causing the loss of many thousands of jobs at those companies and reverberating throughout the industry at the cost of many thousands more. The disappearance of GM in particular—with its roughly 100,000 American employees and its central place in the chain of suppliers, parts manufacturers, and dealers—would have marked the end of the American automobile industry. “If GM were to go into a free-fall bankruptcy and didn’t pay its trade debts, then the entire domestic auto industry shuts down,” one industry analyst told Time magazine in November 2008. Just before the bailouts, reporters heard much the same case made by officials in the Bush administration.

But this nightmare scenario was never likely to happen. In the absence of a bailout, GM and Chrysler would each have been forced to file for bankruptcy like any other company in their circumstances. It is possible that Chrysler would have then faced liquidation (though even this is questionable, given the value of its assets and its brands). General Motors, however, would almost certainly have been re-organized. In all likelihood, this re-organization would have produced a company more competitive than the one that emerged from the bailout process.

Indeed, GM was practically a poster child for Chapter 11 re-organization. The roots of our approach to such re-organization go back to the 19th century—when creditors of railroads that were unable to meet their debt obligations threatened to tear up the rail companies’ tracks, melt them down, and sell the steel as scrap. Innovative judges, lawyers, and businessmen recognized that creditors would collect more over time if they all agreed instead to reduce their claims and keep the railroads running, thus allowing the companies to produce revenues to pay off their debts. This same logic animates Chapter 11 of the bankruptcy code today.

To understand why GM was an obvious candidate for Chapter 11 re-organization (rather than liquidation), it is important to start with the fundamental issue facing any firm filing for bankruptcy—the question
of whether it is “economically failed” or simply in “financial distress.” In deciding between the two, one considers whether it would be most efficient to continue to deploy the company’s assets — its financial, physical, and human capital — by re-organizing, or instead to liquidate the company and allow those assets to be redeployed elsewhere in the economy. For example, if a typewriter manufacturer were to file for bankruptcy today, it likely would be considered an economically failed enterprise: The market for typewriters is small and shrinking, and the manufacturer’s financial, physical, and human capital would probably be better used elsewhere (perhaps in making computers). A financially distressed enterprise, on the other hand, is worth more alive than dead: It may have fallen on hard times — the result of mismanagement or an economic downturn, perhaps — but still provides a product or service that is in demand (and so could someday make for a thriving firm). Through the use of Chapter 11, such a company can continue to operate while re-organizing to get out from under its debts.

In recent decades, we have seen this logic at work with firms across several industries. Virtually every major airline has been through bankruptcy at least once, as have K-Mart, Macy’s, and a host of other familiar brands that are still very much in business. Others have filed for bankruptcy and disappeared — Montgomery Ward, TWA, and Enron, for instance, were found to be economically failed and so were liquidated. Since the onset of the Great Recession in 2008, we have seen this process replicated many times: Numerous retailers (like Crabtree & Evelyn and the Boscov’s department-store chain) have successfully streamlined operations and re-organized under Chapter 11, while other well-known retailers (such as Circuit City and Linens ’n Things) have shuttered their stores.

In late 2008, General Motors was a classic case of a financially distressed rather than an economically failed enterprise. It had a skilled and experienced work force, a stable of longstanding and well-respected brands, and an extended system of relationships with suppliers and customers — all of which illustrated both its underlying value and potential. But the company also had several major financial liabilities: expensive labor contracts, massive legacy costs for pensions and health care, and an outdated and overgrown distribution system of dealerships that needed to be streamlined. A Chapter 11 re-organization would have given GM an opportunity — perhaps its only opportunity — to cut loose this dead weight.
The only obstacle to such a restructuring might have been the requirement that a re-organizing company obtain so-called “debtor in possession” financing—loans of funds it can use in the actual process of re-organization, and which receive first priority in repayment. Some have argued that, in light of GM’s size and the instability in the credit markets at the time, the automaker might not have been able to secure such loans.

While this may be true, a reasonable argument could be made that, under those circumstances, it would have been appropriate to use funds from the Troubled Asset Relief Program to lend or guarantee debtor-in-possession financing to GM. After all, the purpose of TARP was to address liquidity problems in lending markets and to stave off bank runs that might have threatened the stability of solvent institutions. And any failure by GM to obtain debtor-in-possession financing would have been attributable to such liquidity problems in the lending markets. Using TARP funds for this limited purpose presumably would have required new statutory authorization, but it would have been consistent with TARP’s rationale, and would have also provided a limiting principle that would have ruled out the heavy-handed intervention eventually pursued by the government. Plus, congressional approval of such a measure probably would have been more forthcoming than approval of a straightforward bailout. Instead, the Bush administration—evidently in a state of panic as the economic crisis continued to mount—pursued a far more open-ended use of TARP funds, injecting billions directly into Chrysler and GM.

Here we encounter the next premise of the success-story narrative: that, in moving to avert a catastrophe in the auto industry, the president made legitimate use of the emergency authority and resources he was granted by Congress to address the economic crisis.

In truth, however, the use of TARP funds to bail out GM and Chrysler most likely violated the law. The Troubled Asset Relief Program authorized the secretary of the Treasury “to purchase…troubled assets from any financial institution, on such terms and conditions as are determined by the Secretary”; the law also gave the Treasury secretary power “to take such actions as the Secretary deems necessary to carry out the authorities” in the legislation. As Boston University law professor Gary Lawson noted in the Harvard Journal of Law & Public Policy last year, the boundaries set on the use of these funds were so vague and so loose as to produce something approaching a slush fund for the Treasury. And
yet, loose as it was, the TARP legislation did not permit the use of the allotted funds to bail out automakers. The car companies, after all, were not “financial institutions.”

Indeed, when the idea of bailing out Chrysler and GM came up, the congressional leadership decided that such a move would require new legislation, even though voting on a bill would necessarily put every member of Congress in a difficult spot. Supporting it would mean backing yet another bailout when the public was already outraged over TARP and the other lifelines to Wall Street, while voting against the legislation would mean declining to help American autoworkers. It is unlikely that Congress would have taken up such a difficult measure if the leaders of the House and Senate thought GM and Chrysler could be helped without a new law.

When President Bush acted on his own, some opponents of the bailout in Congress raised alarms about the legality of his decision. A group of 26 irate Republican lawmakers sent a sharp letter to the president complaining that “Congress never voted for a federal bailout of the automobile industry, and the only way for TARP funds to be diverted to domestic automakers is with explicit congressional approval.” Supporters of the bailout kept mum about the question of legality.

For its part, the September 2009 report of the Congressional Oversight Panel of TARP noted that the question of the basic legality of the auto bailout was one of “considerable debate” characterized by significant “ambiguity” in the legislative language and congressional intent. But the panel cited no specific instance of “ambiguity,” and it is very hard to see how a bailout of automakers could have been the intent of the original TARP legislation — let alone to see how the letter of the law could be read to permit such use of TARP dollars.

Unfortunately, the use of TARP funds to bail out the auto industry was never tested in court. Although a challenge was raised by some of Chrysler’s creditors as part of the company’s bankruptcy case, the bankruptcy court refused them standing on that issue (arguing that the particular mechanism behind the bailout was not relevant to their claims). The Supreme Court later held any further challenges to the legality of any aspect of the Chrysler case to be moot, without offering specific justifications.

The bailouts of GM and Chrysler at the end of 2008 — and the extension of those bailouts in the beginning of 2009 — were therefore
both unnecessary and very likely illegal. But that was hardly the end of the story.

**The Bankruptcy**

After the bailouts came the arranged bankruptcies. At first, when the government announced that Chrysler and General Motors would be filing for Chapter 11, the news was received with relief by the market, the companies’ creditors, and everyone concerned for the rule of law. The mess created by the bailout could finally begin to move from the political arena to the legal arena, and so regain some semblance of legitimacy and order.

But it wasn’t long before these hopes were dashed by the government’s management of the process. Instead of a regular bankruptcy proceeding, the Obama administration, working with the automakers, patched together a process without precedent—a bankruptcy combined with a bailout, incorporating the worst elements of both.

Of the two proceedings, Chrysler’s was clearly the more egregious. In the years leading up to the economic crisis, Chrysler had been unable to acquire routine financing and so had been forced to turn to so-called secured debt in order to fund its operations. Secured debt takes first priority in payment; it is also typically preserved during bankruptcy under what is referred to as the “absolute priority” rule—since the lender of secured debt offers a loan to a troubled borrower only because he is guaranteed first repayment when the loan is up. In the Chrysler case, however, creditors who held the company’s secured bonds were steam-rolled into accepting 29 cents on the dollar for their loans. Meanwhile, the underfunded pension plans of the United Auto Workers—unsecured creditors, but possessed of better political connections—received more than 40 cents on the dollar.

Moreover, in a typical bankruptcy case in which a secured creditor is not paid in full, he is entitled to a “deficiency claim”—the terms of which keep the bankrupt company liable for a portion of the unpaid debt. In both the Chrysler and GM bankruptcies, however, no deficiency claims were awarded to the wronged creditors. Were bankruptcy experts to comb through American history, they would be hard-pressed to identify any bankruptcy case with similar terms.

To make matters worse, both bankruptcies were orchestrated as so-called “section 363” sales. This meant that essentially all the assets of “old
Chrysler” were sold to “new Chrysler” (and “old GM” to “new GM”), and were pushed through in a rush. These sales violated the longstanding bankruptcy principle that an asset sale should not be functionally equivalent to a plan of re-organization for an entire company—what bankruptcy lawyers call a “sub rosa plan.” The reason is that the re-organization process offers all creditors the right to vote on the proposed plan as well as a chance to offer competing re-organization plans, while an asset sale can be carried out without such a vote.

In the cases of GM and Chrysler, however, the government essentially pushed through a re-organization disguised as a sale, and so denied the creditors their rights. As the University of Pennsylvania’s David Skeel observed last year, “selling” an entire company of GM or Chrysler’s size and complexity in this manner was unprecedented. Even on a smaller scale, it would have been highly irregular: While rush bankruptcy sales of much smaller companies were once common, the bankruptcy laws were overhauled in 1978 precisely to eliminate this practice.

At first, the fact that the companies’ creditors (and especially Chrysler’s creditors, who were so badly mistreated) put up with such terms and waived their property rights seems astonishing. But it becomes less so—and sheds more light on how this entire process imperils the rule of law—when one considers the enormous leverage the federal government had over most of these creditors. Many of Chrysler’s secured-bond holders were large financial institutions—several of which had previously been saved from failure by TARP. Though there is no explicit evidence that support from TARP funds bought these bond holders’ acquiescence in the Chrysler case, their silence in the face of a massive financial haircut is otherwise very difficult to explain.

Indeed, those secured-bond holders who were not supported by TARP did not go nearly as quietly. A group of hedge funds that were among Chrysler’s creditors initially objected to the bailout plan that preferred the UAW at their expense. In a now-infamous speech in April 2009, President Obama publicly attacked these investors—who were merely standing up for their contract and property rights—as profiteers, criticizing them for their unwillingness to make the same sacrifices as other investors (but not, of course, UAW members, who received a windfall). In response to this public browbeating from the president of the United States, the hedge funds caved and agreed to the terms. In the end, only one group of Chrysler bond holders—the
Indiana state teacher and police pension funds—continued to object. Indeed, they objected at every stage of the process, but the Supreme Court declined to hear their case.

General Motors, too, had issued secured debt during its years of financial turmoil, but these bonds made up a far smaller fraction of the company’s total outstanding debt. And in striking contrast with the Chrysler case, General Motors’s bankruptcy plan left the secured creditors intact, paying them the full value of their claims. From the perspective of bankruptcy law and contract rights, this development was encouraging: The Obama administration did not seek to plunder GM’s secured creditors as it had Chrysler’s. From the perspective of the rule of law, however, this differential treatment might have been even more troubling.

On the matter of secured-bond holders, the cases of GM and Chrysler were functionally indistinguishable—and yet GM’s secured creditors were treated far better than Chrysler’s. The administration offered no public justification for this differential treatment, and to an outside observer, there was only one key difference between the cases: The amount of GM’s secured debt was relatively small compared to Chrysler’s. The obvious conclusion, then, is that the difference in how the government treated the automakers’ creditors was purely a matter of expediency—hardly a justifiable rationale.

**GOVERNMENT MOTORS**

The highly irregular bankruptcies and re-organizations of General Motors and Chrysler left the White House and Congress with enormous power over the subsequent operations of both companies. (This was especially true of GM, in which the government at first had a majority stake, and in which it still possesses about one-third of the common stock.)

Some government interventions were relatively subtle—the companies’ increased emphasis on hybrids and electric vehicles, for instance, which are Obama-administration priorities but hardly sound economic choices for troubled automakers. But other interventions were quite egregious—especially those related to the automakers’ decisions about closing dealerships.

Because of state laws that are highly protective of auto dealers, terminating and closing dealerships can be extremely difficult and expensive. It has been estimated, for example, that it cost General Motors more than
$1 billion to close dealerships when it decided to terminate its Oldsmobile line in 2004. Bankruptcy provided the opportunity to cut through this red tape by pre-empting those state laws, and so offered the automakers a valuable chance to streamline—which is, of course, the very purpose of bankruptcy re-organization.

Unfortunately, the automakers came up against the same force that produced those protective state laws in the first place: the auto-dealer lobby, which wields enormous political influence (especially in small towns and rural areas). Indeed, in many congressional districts, auto dealers are among the most high-profile members of their communities; they sponsor Little League teams, support local charities, and host political fundraisers. It was therefore not surprising that Washington politicians were so aggressive in their efforts to reverse GM’s decisions about dealership closures. Senator Amy Klobuchar, for instance, persuaded GM to rescind a closure order for a large dealership in Bloomington, Minnesota. Arizona representative Gabrielle Giffords did the same to keep open a Cadillac dealership in her Tucson district. Senator Jay Rockefeller intervened to rescue a dealership in West Virginia, and Senator Charles Schumer and Representative Dan Maffei intervened to save a Cadillac dealership in Syracuse, New York.

In addition to these ad hoc interventions, Congress passed a law in December 2009 giving terminated dealers special rights in seeking arbitration—a process that has burdened GM with substantial delays and costs. According to an August 2010 report in Automotive News, of cases that had actually gone to arbitration, GM had won 39 and lost 23. Furthermore, the company had entered into letters of intent for conditions for reinstatement with 702 other dealerships. Taken together, those dealers reinstated through arbitration and those offered reinstatement through letters of intent represented 62% of all the dealers that had filed claims for arbitration. In addition, GM had settled disputes with 458 dealers under undisclosed terms; according to lawyers for the dealers, however, the dealerships were usually terminated only after GM paid case settlements—settlements that, in some instances, reached as high as several million dollars. The result of the 2009 law has thus been an unimpressive arbitration record for General Motors, and the retention of many more dealerships than sound business principles could justify.

Such political pressures were exerted on behalf of suppliers, too. For instance, GM had for several years purchased the mineral palladium
from a Montana mine; upon filing for bankruptcy, the company decided to replace the Montana distributor with cheaper suppliers in Russia and South Africa. But Montana’s senators, Democrats Max Baucus and Jon Tester, prevailed upon GM to abandon its plans and continue using the more expensive Montana supplier. Similarly, when GM announced plans to produce a new subcompact car in China, immense pressure from Capitol Hill forced the company to reverse its decision.

Arriving at more efficient dealership arrangements and more cost-effective relationships with suppliers was, of course, one of the chief reasons given for putting the automakers into bankruptcy. But these aims were seriously undercut by the meddling of elected officials. There is little doubt that General Motors—and, in all probability, Chrysler too—would have emerged stronger and more competitive had they pursued normal bankruptcies (perhaps with some help in obtaining financing), not massive bailouts followed by bankruptcies run by the government.

STATE CAPITALISM

Every piece of the “success story” of the auto bailout would thus seem to be in error. The bailout was not absolutely necessary and was pursued by means of dubious legality; the bankruptcies were highly irregular and inefficient; and the companies that have emerged from bankruptcy are far from lean and fit. They are certainly in no position to repay taxpayers for the generous loans they were given.

But as bad as the facts of the story are, the implications are much worse. Through their actions, both the Bush and Obama administrations have set dangerous precedents—and made it much more difficult to reverse the trends of executive overreach and excessive government entanglement with private business.

As a matter of policy, the Bush interventions early in the process were more ad hoc affairs, motivated largely by panic in the midst of the economic crisis. This was particularly true of Treasury Secretary Henry Paulson, whose performance in the final months of the Bush administration was disgraceful. But it is hard to avoid the conclusion that, at its core, the Bush approach was also influenced by the imperious view of executive power that had developed in the course of the war on terror and had been supported by some conservative thinkers for much of Bush’s presidency. The notion that the president simply must do whatever he judges necessary in an emergency—regardless of whether he has
the formal legal authority to do it—is among Bush’s foremost legacies. The concluding months of his presidency should offer a cautionary tale to conservatives inclined to adopt that view of executive power.

The Obama administration’s role in this story, however, is far more troubling. One cannot explain away Obama’s overreach as a panicked response to an emergency; rather, his actions toward GM and Chrysler were part of a considered, coherent approach to the relationship between government and private industry. And this approach—defined by broad government power unchecked by legal constraints and possessing sweeping authority to pick winners and losers—has guided the administration’s policies well beyond the auto bailout. The aim of this approach is to rejuvenate the New Deal vision of the regulatory state, in which regulators are seen as disinterested experts with the factual knowledge, practical wisdom, and unwavering integrity to manage the economy. They alone are presumed to be capable of steering the nation toward prosperity.

It was this approach that clearly animated, for instance, the financial-reform legislation enacted by President Obama and the Democratic Congress last year. Just as the government was seen as having the wisdom to micromanage the restructuring of Chrysler and General Motors, so the new financial-reform law creates a vast web of regulatory bodies and presumes that they will have the know-how to successfully reshape America’s entire financial system. The same basic pattern can be seen in several of the Obama administration’s other legislative achievements—from the massive 2009 stimulus package to the healthcare reform bill to a host of environmental regulatory initiatives.

Taken together, these laws have dramatically worsened the entanglement of government and the private sector, and have thereby led to an increase in lobbying activity by special interests seeking government favors or protection. The financial-reform law, for instance, is littered with special-interest provisions intended to entice major corporations into supporting the administration’s new approach to economic policy. Auto-finance lenders are inexplicably exempted from the jurisdiction of one of the law’s new creations, the Consumer Financial Protection Bureau, thereby sparing them (and the influential auto dealers they work with) from the regulatory costs and hassles caused by the CFPB. The nation’s biggest banks, too, ultimately came to support the creation of the CFPB, as they recognized that its heavy regulatory burdens would be borne much more easily by large institutions—which can more readily afford to
hire lobbyists and lawyers to help navigate the law’s complexities—than by their smaller competitors.

Other examples abound; among them, the most outrageous is probably the sweeping health-care law enacted last year. The legislation had the support of America’s major health insurers—likely because the law made them the first suppliers in American history to see the federal government mandate the purchase of their product by every single citizen. The opposition of pharmaceutical manufacturers, too, was significantly dampened; presumably this had something to do with the administration’s promises of increased market demand for their products. Even the American Medical Association—which should have been representing the interests of doctors, who will face enormous difficulties under the law—rolled over, partly to obtain a repeal of rules that had limited certain Medicare reimbursements. Again and again, large corporate actors and other organizations have been willing to sell some freedom of action in return for a competitive advantage provided by the government.

**Managed Decline**

The Obama administration’s economic policy, therefore, returns us to the thinking of the 1950s and ’60s—to an economy in which big business, big labor, and big government are tied together in a relationship of mutual succor and support.

The auto bailouts exemplify this new reality. Sold as a means of revitalizing the economy, they are in fact a means of transforming the relationship between the state and the market in a way that empowers large players at the cost of economic growth. The overall effect of such state capitalism is a kind of controlled stasis, in which the preservation of old jobs takes priority over the creation of new ones. Managed decline, rather than dynamic growth, is the defining feature of the Obama economy.

It is not hard to understand why those who embrace this vision of politics and economics would see the bailouts of Chrysler and General Motors as a great success story. But their notion of success is a far cry from old-fashioned prosperity. The Obama administration’s idea of what is good for General Motors, much like its idea of what is good for America, is unlikely to be particularly good for either.