Center for American Progress

AP PHOTO/MARK LENNIHAN

Unbundling 'Too Big to Fail'

Why Big Is Bad and What to Do About It

By Ganesh Sitaraman July 2014

Introduction and summary

Since the 2008 financial crisis, the problem of financial institutions being "too big to fail," or TBTF, has been front and center in the public debate over the reform and regulation of the financial industry. Commentators across the political spectrum decried bailouts of the biggest Wall Street financial institutions, arguing that bailouts would establish too big to fail as public policy. When it was time for reform, legislators tried to address this problem, and even incorporated into the full title of the Dodd-Frank Act that one of the bill's purposes was "to end 'too big to fail.'"[1]

Yet more than five years after the financial crash, the biggest banks are 37 percent larger than they were before,[2] and the debate over what to do about the size of financial institutions continues. Policy proposals range from improving resolution mechanisms, to more stringent prudential standards such as leverage limits, to charging fees to eliminate the implicit government subsidy the biggest banks receive, to capping the size of the banks, to instituting a new Glass-Steagall Act. Each approach is hotly contested, with commentators frequently arguing that the proposed solution will not actually fix the problem of financial institutions that are too big to fail.[3]

The problem at the heart of the debate over too big to fail is that the popular moniker has come to mean more than the concern that big firms get a government bailout in the event of failure. It captures a variety of concerns with the financial industry: economic, competitive, systemic, firm level, political, legal, and regulatory. This report identifies the full range of reasons reformers might be worried about TBTF. It then describes the various policy options that are most frequently discussed with regard to reforming TBTF, and it connects the specific reforms to the concerns they address.

To make progress, reformers and critics alike need to engage in a more precise debate. Critics too often dismiss reforms without fully addressing the concerns reformers seek to address, and when outlining proposals, reformers could be clearer about the problems they seek to solve. Ultimately, people will disagree about what aspects of TBTF are most concerning to them. But the first step toward a more meaningful debate over reform requires greater clarity about the particular concern—or concerns—with big financial institutions and the specific solutions that address those concerns.

The Center for American Progress is a nonpartisan research and educational institute dedicated to promoting a strong, just and free America that ensures opportunity for all. We believe that Americans are bound together by a common commitment to these values and we aspire to ensure that our national policies reflect these values. We work to find progressive and pragmatic solutions to significant domestic and international problems and develop policy proposals that foster a government that is "of the people, by the people, and for the people."

Center for American Progress

1333 H STREET, NW, 10TH FLOOR, WASHINGTON, DC 20005 • TEL: 202-682-1611 • FAX: 202-682-1867 • WWW.AMERICANPROGRESS.ORG