

“Upending the New Deal Regulatory Regime:  
Democratic Party Position Change on Financial Regulation”

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Abstract: Why did Congressional Democrats upend the financial regulatory regime they had maintained since the New Deal? I argue that the congressional reforms of the mid-1970s paved the way for the Democratic Party’s turn against financial regulation. Prior to congressional reform, Democrats in Congress were especially parochial, and southern populists dominated the House and Senate banking committees. These parochial and populist orientations complemented the radically decentralized banking system by New Deal financial regulations. The elimination of the seniority rule and other reforms reduced parochialism and strengthened Democratic leadership, enabling the party to enact deregulatory reforms that provided (short-term, at least) benefits to the diffuse interests of American savers and consumers at the expense of entrenched local industry groups. In the long run, however, these deregulatory reforms significantly accelerated the concentration of economic power held by the nation’s largest firms and wealthiest individuals.

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New Deal financial regulations buttressed a radically decentralized system of small local banks by mitigating “cutthroat” competition, constraining interest rates as well as bank mergers and acquisitions, and imposing a firewall between commercial and investment banking (i.e. Glass-Steagall). For nearly half a century, the Democratic Party preserved this New Deal regulatory regime, and stymied encroachment from Wall Street firms determined to move American savings and debt out of local depository institutions and into more volatile securities markets. However, the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) and the Garn-St. Germain Depository Institutions Act of 1982 (GSDIA) fundamentally upended the New Deal regulatory regime by removing interest rate restrictions, placing savings and loans (S&Ls) and commercial banks in direct competition, enabling greater consolidation in the industry and significantly eroding Glass-Steagall.

Even a sophisticated observer of American politics may be forgiven for assuming that Republicans were the chief architects of financial deregulation, but this is not the case. DIDMCA was sponsored by Fernand St. Germain, the soon-to-be Democratic chair of the House Banking, Finance, and Urban Affairs Committee, advanced to the floor by Democratic Party leaders in both chambers, supported by overwhelming majorities of House and Senate Democrats on the floor, and signed into law by Jimmy Carter. Twenty-seven of the 28 cosponsors of GSDIA were Democrats, including future party leaders Chuck Schumer and Steny Hoyer, and the bill was supported by the party leadership and Democratic majorities in both chambers. Democrats did not reluctantly consent to a Republican plan to deregulate the financial industry; rather, the Democratic Party initiated financial deregulation.

This is the most important case of the Democratic Party's general repositioning on economic regulation since the 1970s. Beginning during the Carter Administration, prominent Democrats played a leading role in retrenching economic regulations that had protected local business and labor interests in the trucking, airlines, energy, and telecommunication industries. Extant research on the politics of economic deregulation attribute these "public interest reforms" to the burgeoning consumer rights movement, and ideological change among liberal intellectuals and officeholders (Derthick and Quirk 1985; Harris and Milkis 1996; Arnold 1990). But why did Democrats align more closely to the national consumer rights movement, despite intense opposition from organized labor and other entrenched industry groups that were active in every congressional district? And why did Democrats come to prioritize the ideals of consumer capitalism and market efficiency despite continued concern among many in the party that an unregulated environment would result in inequality and the concentration of economic power?

I argue that changes in congressional institutions—independent of shifting interest group alliances and ideological concerns—functioned as a crucial causal factor behind Democrats' rapid and substantial position change on economic regulation. From the New Deal to the mid-1970s, a decentralized institutional structure in Congress oriented Democratic legislators towards the local concerns of their district. In this institutional context, constituent-centered Democrats preserved the financial regulations that buttressed the nation's radically decentralized system of small local banks and S&Ls. However, as a result of the congressional reforms of the 1970s, the Democratic Party became more centralized as party leadership gained greater control over committees and the legislative process. Speaker Tip O'Neill used these new institutional powers to

champion President Carter's deregulatory agenda, despite the continued lobbying from entrenched interest groups, in an effort to promote the party's brand by enacting laws that provided immediate benefits to American savers and consumers. This effort to advance what Arnold (1990) would consider "public interest legislation" would have been unlikely to occur absent the prior reorganization of congressional institutions.

In the first analytical section of this article, I sharpen the puzzle of Democrats' position change on financial regulation by demonstrating the limitations of the prevailing theoretical and empirical work on political parties and partisan position change. A fruitful body of research argues that parties strategically make political and policy decisions to maintain support among intense policy demanding groups ensconced within the party coalition, or to consolidate support among crosscutting groups (Karol 2009; Cohen et al. 2008; Bawn et al. 2012; Schlozman 2015; Hacker and Pierson 2014; Hacker et al. 2021). I test this hypothesis by analyzing interest group testimony during congressional hearings on financial deregulation. I find that Democrats dismantled central New Deal financial regulations in the early 1980s despite intense *opposition* from their core interest group ally (organized labor) and the entrenched crosscutting groups who benefitted from these policies (small banks, S&Ls, real estate brokers and construction firms). DIDMCA and GSDIA most closely aligned to the demands of Wall Street and (to a lesser extent) consumer advocacy organizations. However, an interest-based account is insufficient for explaining why, in the 1980s, Democrats finally pivoted against regulations that Wall Street had opposed for decades.

Next, I develop my theory on the effects of congressional reform. In the second analytical section of the article, I construct a legislative history of the most consequential financial deregulation bill, DIDMCA (1980), using a wide variety of qualitative data sources including Banking Committee correspondence and internal documents acquired through original archival research, testimony from committee hearings, markup sessions and the Congressional Record, periodicals, and a close reading of legislative bills. I find that, after the House Banking Committee repeatedly failure to pass the most consequential deregulatory provisions of DIDMCA in markup sessions, the newly empowered Democratic Party leaders managed to pass the bill on the House floor through a combination of unorthodox procedures that forced the House to vote on the complete package without amendments, hid the most controversial deregulatory provisions, and insulated rank-and-file Democrats from interest groups opposition. Such procedural maneuvers were necessary for the enactment of robust financial deregulation in 1980, and would have been impossible or unimaginable in the pre-reform House.

In the third analytical section, I test the effects of district-level industry and demographic variables on an original measure of members' roll call voting that captures support for financial deregulation. I find that up to the period of congressional reform, members from districts with more union representation and a less concentrated banking industry (i.e. more small local banks) were especially likely to maintain support for the New Deal regulatory regime and vote against deregulatory reforms. However, after congressional reforms undercut southern committee chairs and centralized power within party leadership, district-level variables became far less predictive of voting behavior on

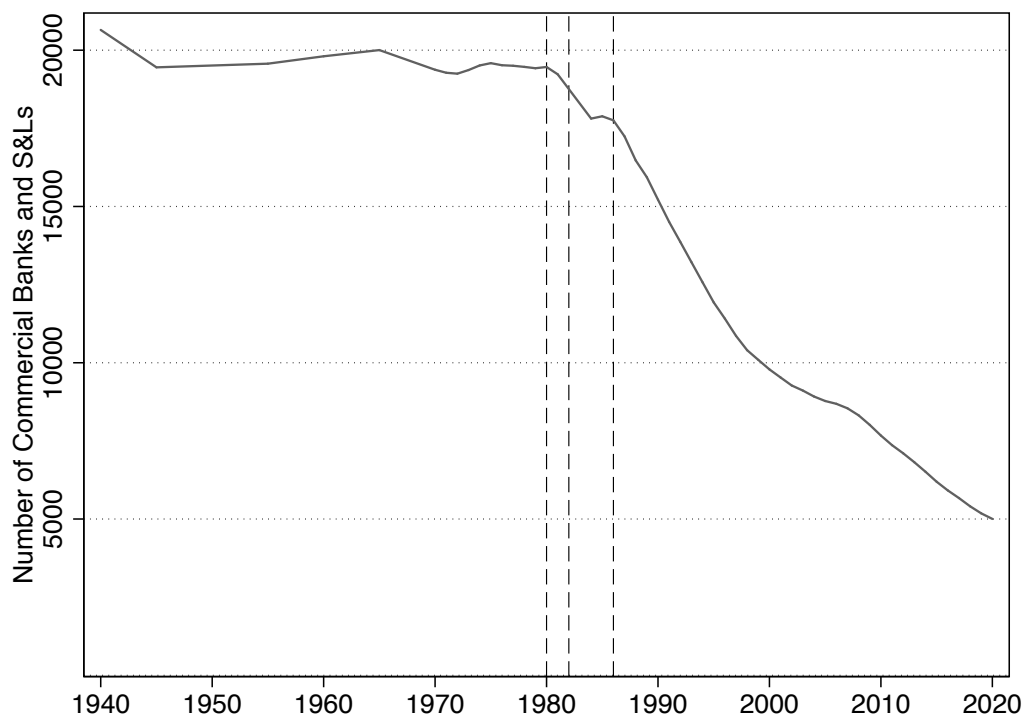
financial regulation. These findings support my theory that congressional reform increased the likelihood of financial deregulation by making Democrats less constituent-centered, as they became more willing to buck entrenched local industry groups that wanted to preserve New Deal financial regulations.

These findings are consistent with the claims made by the prominent mid-twentieth century proponents of the “Responsible Parties Thesis,” who argued that stronger parties in government would advance their collective interest in winning or maintaining power by enacting policies that benefit the diffuse interests of the general public, rather than simply catering to the parochial interests of well-organized groups (Key 1964; Schattschneider 1942; APSA 1950; Ranney 1962). Under the conditions of hyperinflation and tight credit markets, the deregulatory reforms championed by Democrats expanded access to credit, and enabled working-class Americans and small businesses to enjoy the higher—albeit far more volatile—rates of return offered by securities markets, at the expense of entrenched industry and labor groups (Davis 2009; Krippner 2011).

However, to the extent that this article demonstrates the promises of stronger party government, it also reveals the benefits of district-centered legislating and pitfalls of centralization in Congress. While financial deregulation made it easier for working- and middle-income Americans to obtain a loan, and increased the rate of returns on their savings, it has also paved the way for the “financialization” of the American economy (Krippner 2011; Witko 2016; Keller and Kelly 2015; Kelly 2019). The movement of Americans’ debt and savings into securities markets fueled the financial industry’s growing dominance over the broader economy. Over the course of the 1980s, finance,

insurance and real estate's (FIRE) share of corporate profits in the U.S. economy *doubled*, and FIRE rapidly eclipsed manufacturing as a share of GPD (Krippner 2011). In contrast to stagnating median incomes in the broader economy, salaries on Wall Street have soared since the 1980s. Moreover, the regulatory unraveling that began in the early 1980s created the conditions for the Great Recession of 2008.

Figure 1: Total Number of Banks and S&Ls Before and After Deregulation



Note: Author's calculation based on FDIC data.

Relatedly, financial deregulation greatly exacerbated the concentration of economic power. As Figure 1 reveals, after half a century of stability, small local S&Ls and commercial banks failed at an astonishing rate, especially after the deregulatory reforms in DIDMCA (1980) and GSDIA (1982) went into full effect in 1986. In response, the nation's largest firms expanded into communities across the country to fill the void—the share of American's deposits held by the nation's 10 largest commercial

banks doubled from 1985 to 1995, and tripled from 1985 to 2005 (Janicki and Prescott 2006).

Moreover, financialization and market concentration in the banking industry fundamentally reshaped corporate behavior in other industries. Wall Street firms and wealthy investors used their growing influence to reorient non-financial industries towards the short-term priorities of shareholders, and away from employees and local communities. Meanwhile, as the largest banks acquired a larger share of the nation's savings, they were able to issue larger corporate loans that could be used for larger and larger mergers and acquisitions (Davis 2009).

This article makes an important contribution to the study of American political economy and inequality. A burgeoning literature on the politics of economic inequality details the rightward turn in public policy since the Reagan Revolution (Hacker and Pierson 2010, 2016; Jacobs and Skocpol 2005). This important body of research largely attributes this policy trend, and the corresponding rise in economic inequality, to the mobilization of economic elites and conservative groups on the right (Prasad 2006; Vogel 1989; Hertel-Fernandez 2013, 2014, 2016, 2019; Skocpol and Williamson 2016; Skocpol and Hertel-Fernandez 2016), and an increasingly conservative and electorally successful Republican Party (Hacker and Pierson 2006, 2010, 2016, 2020; Bartels 2008). By contrast, this article showcases the how the Democratic Party initiated reforms that fundamentally restructured the American economy, and greatly exacerbated inequality over the last several decades.



## **New Deal Regulatory Regime**

New Deal financial regulations created a set of entrenched interests that represented a sizable share of the American economy, and fought to preserve these policies, in large measure, through the Democratic Party. Glass-Steagall separated depository institutions and investment banks by prohibiting investment firms from offering interest payments on deposits. This provision buffered ordinary Americans from the whims of markets, and ensured that credit was available for local mortgages and business loans. By building a firewall around the debt and savings of middle- and working-class Americans, Glass-Steagall constrained more lightly regulated securities brokers and investors from speculating with the burgeoning savings and debt of American consumers. It also had the effects of buffering small, local commercial banks and savings and loans (S&Ls) from direct competition with investment firms, which were generally large, national institutions located in metropolitan cities.

While Glass-Steagall protected local commercial banks and S&Ls from competition from national investment banks, complementary New Deal policies substantially minimized competition among commercial banks and S&Ls. The most important of these was a Federal Reserve rule, created in accordance with the Banking Act of 1933, called Regulation Q, which set limits on the interest rate commercial banks and S&Ls could offer depositors for their savings. When the original legislation was drafted during the Great Depression, Regulation Q was intended to prevent future bank runs and speculative lending. In practice, Regulation Q functioned much like a price control. By setting a ceiling on the interest rate banks and S&Ls could pay their depositors, small local banks could limit their expenses (i.e. interest payments) without

worrying that a competitor would lure away their customers by offering higher interest rates on deposits. Since larger financial institutions had the excess capital to survive rate wars, it was widely accepted that Regulation Q benefitted the small- and medium-sized local banks and S&Ls, which constituted the overwhelming majority of depository institutions in the mid-20<sup>th</sup> century (Brandeis 1915; Kaufman 1986; Krippner 2011).<sup>1</sup>

Still another set of policies limited competition between banks and S&Ls. Only commercial banks were permitted to offer checking accounts, but in an effort to reduce the attractiveness of checking accounts in relation to S&Ls accounts, banks were prohibited from paying interest to depositors in these highly convenient and liquid accounts. Moreover, lawmakers also imposed what became known as the “differential,” which provided an advantaged to S&Ls by allowing them to offer slightly higher interest rates than commercial banks and savings accounts. Meanwhile, various regulations successfully encouraged commercial banks to specialize in business loans, while S&Ls predominately issued mortgages.

The New Deal regulatory regime ensured that commercial banks would mostly serve local businesses, S&Ls would mostly serve individual savers and homebuyers, while investment firms would serve wealthy individuals and large corporations. Small and medium-sized commercial banks and S&Ls favored these anticompetitive regulations. Local bankers during this period would joke that they lived by the 3-6-3 rule: pay 3% interest to depositors, lend those deposits to borrowers at a rate of 6%, and make it to the golf course by 3pm (Zweig 1995).

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ional safeguards to protect the decentralized system of banking, and ensure that credit would remain local.

But the entrenched defenders of the New Deal regulatory regime extended far beyond the banking industry. Since local depository institutions were highly restricted in their ability to invest member deposits outside of the community, banks and S&Ls predominately issued loans for local business and home construction. Consequently, local real estate agents, developers, construction firms and labor unions across the country consistently allied with small- and medium-sized commercial banks and S&Ls to preserve these financial regulations.

### **Economic Crisis and Early Financial Deregulation**

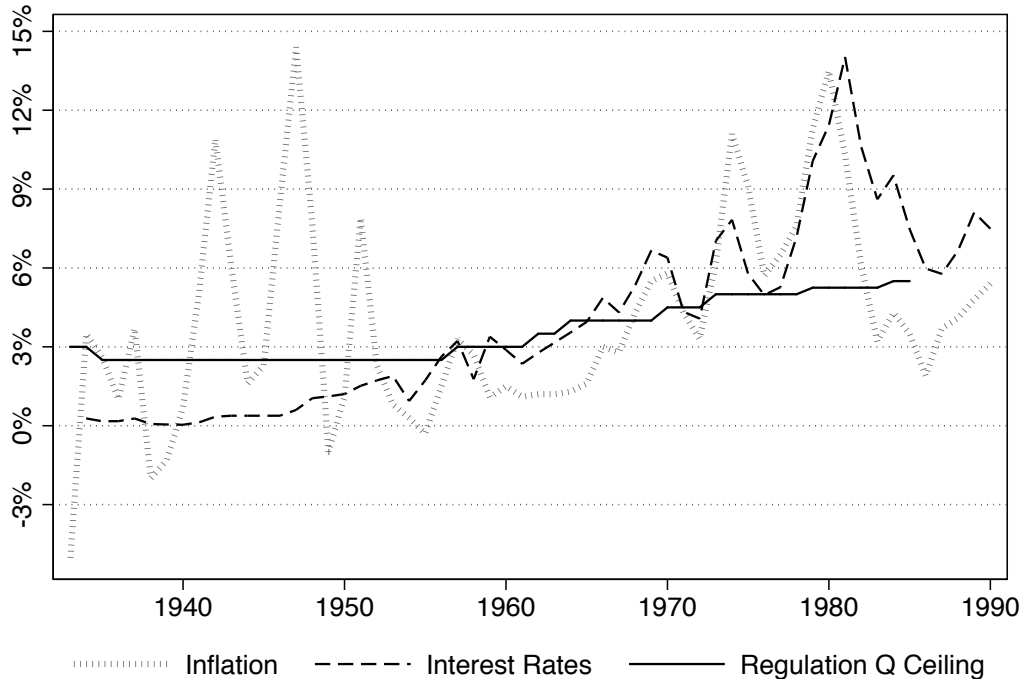
Regulation Q imposed tolerable costs on ordinary savers so long as inflation generally remained low, and period of high inflation were short-lived. However, Regulation Q became truly burdensome during the inflation crisis of the 1970s. As Figure 2 shows, from the late 1960s into the early 1980s, inflation rates mostly exceeded the ceiling rates imposed by Regulation Q. Even though policymakers elevated the maximum rate commercial banks and thrifts could offer depositors multiple times during this period, depositors were unable maintain the real value of the savings. When inflation exceeded 13% in the late 1970s, the purchasing power of a depositor's savings was depreciating at an annual rate of over 7%.

The combination of Regulation Q and Glass-Steagall froze credit markets and significantly hampered the ability of Americans to earn rates of return that kept pace with inflation (Nocera 1994).

In response, Congress enacted the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) and the Garn-St. Germain Depository

Institutions Act of 1982 (GSDIA), which entirely upended the New Deal regulatory regime and revolutionized American banking and finance.

Figure 2: Inflation and Interest Rates, and Ceiling Rates under Regulation Q



Sources: Federal Reserve Bank of St.Louis; Bureau of Labor Statistics

DIDMCA and GSDIA removed numerous barriers to competition between and among distinct types of financial institutions. First, and most significantly, DIDMCA removed the Regulation Q ceiling on the interest rates that banks and S&Ls paid depositors. While Regulation Q allowed depository institutions to remain competitive while offering only modest interest rates, this reform enabled them to compete by offering higher rates of return.

Second, DIDMCA permitted all depository institutions to provide interest-bearing negotiable order withdrawal (NOW) accounts with check-writing capacity. Previously, S&Ls exclusively offered savings accounts, while commercial banks were significantly constrained in the interest they could offer depositors in checking accounts.

Third, GSDIA explicitly authorized Money Market Mutual Funds (MMFs), which were investment funds for small savers (offered by investment banks) that had the functionality of immediately withdrawal checking accounts. MMFs circumvented Regulation Q and pretty clearly violated the spirit of Glass-Steagall (Nocera 1994; Kaufman 1986). During the 1970s, Congress showed signs that it would bring MMFs into regulatory parody with traditional depository accounts, and thereby mitigate the effectiveness of these funds, or perhaps even ban them altogether.<sup>2</sup> Instead, GSDIA explicitly authorized MMFs without applying reserve requirements.

If banks and S&Ls were to compete by paying out higher rates on deposits, they would need greater flexibility to make money. Thus, the deregulation of banking liabilities was coupled with the deregulation of asset powers.<sup>3</sup> Democrats in Congress did this by implicitly sanctioning variable-rate mortgages (VRMs). Moreover, DIDMC also exempted mortgage, business and agricultural loans from state usury laws. These reforms allowed depository institutions to charge significantly more for credit, and to effectively index loan rates to the federal fund rate, and thereby increase the cash flow from borrowers as the cost of interbank borrowing increased.

DIDMCA and GSDIA were clearly enacted as a response to the economic crises of the 1970s. However, it would be wrong to simply treat Democrats' turn against the New Deal regulatory regime for finance as an apolitical administrative solution to these problems. As contemporary inaction on climate change and economic inequality clearly demonstrate, even severe crises do not necessarily complex congressional action.

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<sup>2</sup> "Money Market Mutual Funds: Hearings Before the *Senate Subcommittee on Financial Institutions*, 96<sup>th</sup> Cong. (1979).

<sup>3</sup> From the perspective of a depository institution, deposits and the interest paid on deposits are liabilities.

Moreover, as we will see, financial deregulation was highly divisive, and a broad array of opponents clearly believed that New Deal financial regulations continued to serve important purposes. Furthermore, Democrats could have (as many advocated) turned to more familiar policy levers in an effort to mitigate hyperinflation—namely, price and wage controls.

### **Policy Demanders During Committee Hearings**

According to the UCLA framework on political parties, position change occurs if groups ensconced within the party coalition issue new demands, or if the party is attempting to consolidate the support of a crosscutting group (Karol 2009). If this framework explains Democrats' pivot on financial regulation, we should observe that Democratic allies or crosscutting groups abandoned their support for the NDRR, or that, during the economic crises of the 1970s, a more electorally crucial coalition mobilized against it.

To test the coalition management theory of party position change on financial deregulation in the late 1970s and early 1980s, I analyze the policy positions of interest groups that were either ensconced within the Democratic Party, or that Democrats might have been attempting to consolidate. For each House and Senate hearing on financial reform that was conducted in the decade before the financial reforms of the early 1980s, I systematically tracked the positions of interest groups on five of the major deregulatory provisions that were included in DIDMCA and GSDIA: 1) the elimination of the Regulation Q interest rate ceiling on deposits, 2) expansion of negotiable order withdrawal (NOW) accounts, which allowed banks and S&Ls to pay interest rates on checking accounts, 3) the sanctioning of money market mutual funds (MMFs) without

regulation, 4) the sanctioning of variable-rate mortgages, and 5) the preemption of state usury laws.

Figure 3 summarizes the positions of entrenched policy demanders on these provisions. I use a plus sign to indicate that the group supported the deregulatory reform, and a negative to indicate the opposition. A plus sign with an asterisk indicates that the group changed positions from opposition or neutrality to support.

Small commercial banks, represented by the Independent Bankers Association of America (IBAA), and small S&Ls, represented by The U.S. League of Savings Associations (USLSA), expressed the most uniform support for the New Deal regulations on bank liabilities. Meanwhile, large S&Ls, represented by the National Savings and Loan League (NSLL) and the Great Western Savings and Loan Association (GWSLA), advocated for the ability to offer checking accounts with interest payments (i.e. NOW).

Figure 3: Positions of Entrenched Interest Groups on Deregulatory Provisions

Policy Demanders	Bank Liabilities			Bank Assets	
	Reg Q Phase Out	NOW Expansion	MMF w/out Regulation	Sanction VRM	Usury Preemption
Small Banks	—	—	—	+	+
Large S&Ls	—	+	—	+	+
Small S&Ls	—	—	—	+	+
Home Builders	—	+*		—	+
Realtors	—	+*		+	+
Organized Labor	—	+*		—	—

The National Association of Home Builders (NAHB), and the National Association of Realtors (NAR), and the AFL-CIO also eventually came around to

supporting NOW accounts. These industries relied on the availability of mortgage credit, and were thus heavily invested in the success of S&Ls. Accordingly, the NAHB and NAR strongly opposed the elimination of Regulation Q, and supported the liberalization of thrift asset powers.<sup>4</sup>

Organized labor clearly believed that deregulating interest rates on deposits would significantly harm the thrift industry, and result in less credit for home building, which would lead to less work for their laborers.<sup>5</sup> In fact, union leaders were generally opposed to deregulating the assets and liabilities of S&Ls, with one important exception: the AFL-CIO supported the expansion of NOW accounts, on the condition that Regulation Q limits would be extended to these accounts.<sup>6</sup>

While entrenched industry groups held distinct positions on some bank liability and asset liberalization, the variation displayed in Figure 3 actually greatly understates

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<sup>4</sup> *Regulation Q and Related Measures: Hearings Before the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance*, 96<sup>th</sup> Cong. (1980)(statements by Roland Ferland, NAHB; and Ralph Pritchard, president of NAR); *NOW Accounts, Federal Reserve Membership and Related Issues: Hearings Before the Senate Subcommittee on Financial Institutions*, 95<sup>th</sup> Cong. (1977)(statements by Roland Ferland, Vice Chairman of NAHB; and Daniel Hanrahan, chairman of Legislative Committee of NAR).

<sup>5</sup> *Regulation Q and Related Measures: Hearings Before the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance*, 96<sup>th</sup> Cong. (1980) (statement by Henry Schechter, Director of the Department of Urban Affairs, AFL-CIO); *NOW Accounts, Federal Reserve Membership and Related Issues: Hearings Before the Senate Subcommittee on Financial Institutions*, 95<sup>th</sup> Cong. (1977) (statement by Henry Schechter, Director of the Department of Urban Affairs, AFL-CIO); *Financial Institutions and the Nation's Economic "Discussion Principles": Hearings Before the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance*, 94<sup>th</sup> Cong. (1975) (statement by Nathaniel Goldfinger, Director of the Research Department, AFL-CIO).

<sup>6</sup> *The Consumer Checking Account Equity Act of 1979: Hearings Before the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance*, 96<sup>th</sup> Cong. (1979) (statement by Henry Schechter, Director of the Department of Urban Affairs, AFL-CIO).



preference homogeneity on the New Deal regulatory regime. Each of these entrenched industry groups had the most intense preference on Regulation Q, and on this provision they were unanimous.

Small commercial banks, and S&Ls of all sizes, insisted that the removal of Regulation Q, and the “differential” rate ceiling for commercial banks and S&Ls, would pose an existential threat to the savings and loans industry. Moreover, industry and labor groups dependent on local lending institutions shared this assessment, and thus lobbied for Regulation Q to prevent what they claimed would be a catastrophic disruption to the mortgage industry, and thus construction and real estate. This broad array of groups made it clear that retrenchment of the interest rates ceiling was *not* a bargaining chip they were willing to exchange for other asset and liability deregulations. A leader of the USLSA, the nation’s largest association of S&Ls, unequivocally articulated this position:

“We would much prefer to keep the differential. We feel we have to keep the differential even with NOW accounts. Clearly, the NOW account is no substitute for the differential. If giving us NOW accounts means further loss of or erosion of the differential on savings accounts generally and the clear elimination of the differential, then we say don’t give them to us.”<sup>7</sup>

If the entrenched crosscutting and ally groups maintained support for the New Deal regulatory regime, perhaps the emergence of new policy demanders explains the Democratic Party’s repositioning on financial regulation.

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<sup>7</sup> Norman Strunk, US League of Savings Associations, NOW House 1979, p.187. By advocating for the “differential,” Strunk is implicitly also demanding the continuation of Regulation Q. If interest rate ceilings are not imposed on depository institutions, then there can be no “differential” between the interest rate imposed on commercial banks and that imposed on S&Ls.

Figure 4: Positions of Other Groups on Deregulatory Provisions

Policy Demanders	Bank Liabilities			Bank Assets	
	Reg Q Phase Out	NOW Expansion	MMF w/out Regulation	Inaction on VRM	Usury Preemption
Investment Firms <sup>8</sup>			+		
Large Banks	+	+	—	+	+
Consumer Activists	+ *	+ *	+ *	—	—
Civil Rights Activists				—	—

As Figure 4 shows, more than any other policy demanding groups, DIDMCA and GSDIA reflected the preferences and interests of large, national financial institutions. Large commercial banks, represented by the American Bankers Association (ABA), and large investment firms like Morgan Stanley, held clear competitive advantages in this new regulatory environment.<sup>9</sup> So did the Democratic Party reposition on financial regulation to consolidate support from Wall Street?

Large commercial and investment banks eventually found allies in the fight for deregulating asset powers among groups with a more sympathetic valence: consumer advocates. In particular, the Gray Panthers and American Association of Retired People (AARP) conducted intensive letter writing campaigns in favor of a quick Regulation Q

<sup>8</sup> Large investment banks remained evasive on most of these provisions, but they strongly endorsed deregulation in general terms. Based on this and the economic benefits deregulation promised for large investment banks, we might infer that they strongly supported most if not all of these provisions.

<sup>9</sup> The American Bankers Association (ABA) boasted that about 90% of the nation's commercial banks enjoyed the benefits of membership, but since the New Deal regulatory regime safeguarded the nation's decentralized system of small community banks from the existential threat of large national banks, it was impossible for the ABA to represent both large and small commercial banks on most important regulatory issues. The ABA toed the line from time to time, but on the most salient and divisive issues it reliably took positions that advanced the interests of the nation's largest commercial banks (Zweig 1995).

phase out, the expansion of NOW accounts, and statutory approval of MMFs. These organizations argued that their members, who were senior citizens dependent on their retirement savings, were watching the value of their wealth dwindle as a result of inflation and the interest rate ceiling.<sup>10</sup>

Did the emergence of consumer rights advocates, as policy demanders for the deregulation of bank liabilities, prompt Democrats to pivot on the New Deal regulatory regime? That is, despite fierce opposition from the many entrenched interests of Regulation Q, Democrats may have perceived that appealing to consumer activists would have helped the party consolidate support among the burgeoning and increasingly pivotal demographic of middle-class suburbanites (Geismer 2015; Cohen 2003), as well as more affluent senior citizens.

There is reason to doubt that consumer advocacy organizations, as policy demanding groups, galvanized the Democratic Party's position change.<sup>11</sup> First, it is not at all clear from the testimony of the consumer advocates that they were willing to trade the deregulation of bank assets for the deregulation of liabilities. Indeed, while most retirees might enjoy net benefits from the regulation of bank assets and liabilities, it was far from clear that such an arrangement would provide net benefits to the average working consumer-saver. After all, most working Americans owe more in debt than they hold in savings. While consumer advocates wanted savers to receive a higher rate of

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<sup>10</sup> *Regulation Q and Related Measures: Hearings Before the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance*, 96<sup>th</sup> Cong. (1980)(statements by Robert Gnaizda, Gray Panthers; and James Hacking, assistant legislative counsel for AARP).

<sup>11</sup> To argue, as I do here, that Democrats made decisions to benefit the diffuse interests of American consumers is not akin to arguing that Democrats catered to the demands of organized consumer advocacy groups.

return on their savings, they remained skeptical that banks would use more liberal loan standards to exploit borrowers. As one consumer advocate presciently warned,

“How many steelworkers, how many autoworkers, how many public service employees, how many people working in any area can commit themselves to a 35-year mortgage with a fluctuating interest rate? As his mortgage goes up, will his employers raise his hourly rate to help meet the unanticipated, inflationary increased cost? If this answer is no, then where does he get the increased money? From another loan? Perhaps a second fluctuating variable mortgage?”<sup>12</sup>

Moreover, in addition to the inclusion of provisions opposed by consumer advocates, the omission of other provisions provides further evidence that Democrats were not merely catering to these groups. For example, while Ralph Nader, the most high-profile consumer advocate, lamented that interest rates ceilings hurt savers and “shielded inept management,” he also worried about enabling a few national banks to get so large that lawmakers would feel compelled to bail them out with taxpayer dollars during an economic crisis, and the implications this moral hazard would have on individual financial decisions. Indeed, this was the principle concern Nader expressed in his testimony:

“When banks become too big to fail, they in effect have an unwritten guarantee that Uncle Sam is going to bail them out. And in times of trouble, where some banks may be considered shakier than others, and where some cities may be going bankrupt, it is quite clear that some depositors or investors in CD’s are going to

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<sup>12</sup> *Variable Rate Mortgages and Regulation Q: Hearings Before the House Committee on Banking, Currency, and Housing*. 94<sup>th</sup> Cong. (1975)(statements by Geno Baroni, president, National Center for Urban Ethnic Affairs). Quoted in Krippner (2011), p. 77.

say, well, let us put the CD in a big New York bank, because that is not going to fail. Uncle Sam will back it up. So why put it in a bank in Topeka, or even a bank in St. Louis, when you can put it in a bank in New York or in the Bank of America in California?”<sup>13</sup>

Nader was cognizant that the elimination of Regulation Q would result in further concentration in the industry, as small banks failed to remain profitable as interest rates on deposits increased, and large national banks moved in to fill the void. Consequently, Nader and other consumer advocates demanded further regulations on bank holding companies, and on interstate and intrastate branching, and prohibitions against S&Ls converting to stock companies. But Democrats largely ignored these demands during the legislative process, and DIDMCA and GSDIA omitted complementary reforms to stymie conglomeration in the post-Regulation Q banking industry.

In sum, the optimal electoral strategy for the Democratic Party’s on financial regulation was ambiguous. On the one hand, we can reasonably assume that Democrats thought that championing financial deregulation would help the party win more support from Wall Street, particularly in the form of campaign contributions (Kelly 2019; Keller and Kelly 2015), and that the party could strategically employ these increased funds to maintain power. On the other hand, from the party’s vantage point during this period, it would have been unclear at best, and arguably unlikely, that the marginal gains from Wall Street would be greater than the electoral costs of alienating other influential cross-cutting groups (i.e. local banks, real estate brokers and construction firms), and weakening a crucial ally (i.e. organized labor).

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<sup>13</sup> Ralph Nader, FINE Hearings, p. 919.

In short, during the 1970s, the Democratic Party unquestionably reoriented its policy prerogatives in favor of large national financial institutions, and to a lesser extent the national consumer movement, at the expense of groups who enjoyed entrenched advantages under the New Deal regulatory regime. However, it seems unlikely that this reorientation was driven by a sheer strategic calculation that catering to Wall Street and consumer advocates would improve the party's electoral fortunes against Republicans.

Rather, it seems as though many congressional Democrats and bureaucrats genuinely believed that deregulating bank liabilities (i.e. eliminating Regulation Q, sanctioning NOW accounts) and eroding Glass-Steagall (i.e. permitting Money Market Mutual Funds) had the potential to provide immediate relief to American savers. Although consumer advocates were wary about deregulating bank assets (i.e. sanctioning variable rate mortgages, usury preemption), Democrats in Congress reasonably assumed that many depository institutions could not remain profitable if banks had to pay market prices for deposits but could not charge market prices for loans. Moreover, Democrats in Congress and regulators reasonably assumed that allowing banks and S&Ls more asset flexibility would benefit consumers by expanding access to credit and the higher returns of securities markets.

### **Congressional Reform**

In the remainder of this article, I argue that institutional reforms in Congress increased the likelihood of significant economic deregulatory reform by empowering the party leadership, and by undercutting the tendency of Democratic legislators to prioritize their constituents' interests over the party's collective interest.

Prior to the 1970s, power in Congress was highly decentralized, and the Democratic Party was a cross-regional alliance that on many issues was highly divided. Due to the widespread disenfranchisement of African Americans in the Jim Crow South, and the Democratic Party's corresponding dominance in southern elections (Valelly 2004), Southerners had longer careers in Congress than northern Democrats and, since the New Deal, had been overrepresented as committee chairs (Key 1964; Rohde 1991). Moreover, given the national Democratic Party's longstanding dependence on the South in maintaining a winning coalition, southern legislators at-times wielded disproportionate influence within the party (Bateman et al. 2018). While agrarian southern Democrats were concerned about the burgeoning federal government, they were also highly suspicious of large corporations and financial institutions located in the north (Brandeis 1914; Schlesinger 1959, 1960). Consequently, southern committee chairs often used their outsized influence to direct national policy towards imposing and preserving constraints on large national banks and industry.

In these highly decentralized Congresses, members generally self-selected into committees (Fenno 1973), and chairpersonships were achieved through tenure (Polsby et al. 1969). Consequently, ambitious politicians in Congress could only advance their careers slowly by repeatedly winning renomination and reelection, as opposed to pleasing party leaders. Under these institutional conditions, congressional Democrats were far more responsive to the concerns of organized groups and citizens in their district than to party leaders or any sense of the party's collective interest.

District-centeredness—long present in Congress, but exacerbated by the relative weakness of party leaders—undermined collective action towards reforms that party

leaders believed would improve market efficiency and advance the diffuse interests of American consumers, since these policies often threatened entrenched local business and labor interests. Moreover, decentralized industries that were widely distributed across states and congressional districts, such as the commercial banking and savings and loans industries, were especially well positioned to achieve legislative support in this parochial environment.

In the early 1970s, congressional reforms consolidated party leaders' authority in Congress and eliminated the seniority rule, thereby ending committee (as opposed to party) dominance in Congress (Rohde 1991; Sinclair 1995, 2012; Zelizer 2003; Bloch Rubin 2017; Schickler 2001). I theorize that these institutional reforms paved the way for financial deregulation by 1) empowering Democratic Party leadership to exercise greater influence over the Banking Committees, and the legislative process, enabling them to set the agenda, hide controversial provisions, and shield members for interest group attacks, and 2) by making rank-and-file Democrats less parochial and more oriented towards the party's collective interests.

To be clear, I conceptualize the institutional reforms that occurred in Congress during the 1970s as a causal factor that operated independent of the ideas and individuals that set them into motion. Congressional reform was the product of the insurgent faction of "New Politics Democrats" who gained prominence in the historic post-Watergate landslide, as freshman legislators coalesced with more veteran reformers in the Democratic Study Group (DSG). This intraparty faction was ideologically distinct from traditional liberal-labor northerners and southern populists (DiSalvo 2012; Rohde 1991; Andelic 2019). However, they reformed Congress to undercut the power of racially



conservative southern committee chairs and empower freshman legislators and other backbenchers, not to achieve particular economic policy goals. The centralization of party leadership and deregulation of the financial industry that began under Speaker Tip O'Neill were unintended consequences (Rohde 1991).

In the following analytical sections, I evaluate institutional reform and ideological change within the Democratic Party as two conceptually distinct hypotheses.

### **Empowered Party Leadership: A Legislative History of DIDMCA**

In this section, I construct a legislative history to demonstrate the effects of institutional change on Democrats' pivot against New Deal financial regulations. I use a wide variety of qualitative data sources including Banking Committee correspondence and internal documents acquired through original archival research, testimony from committee hearings, markup sessions and the Congressional record, periodicals, memoirs, secondary texts, and a close reading of legislative bills.

Prior to 1975, Wright Patman (D-TX), a southern populist who was overtly hostile to large financial institutions, and the technocratic administrators who sided with them, chaired the House Committee on Banking and Currency.<sup>14</sup> Patman, who spent his freshman term in the House responding to the Great Depression and found a close mentor in Louis Brandeis, dedicated his career to using federal banking regulations to disrupt the concentration of economic power. Patman's counterpart in the Senate was John Sparkman (D-AL), another prominent southern populist.

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<sup>14</sup> For example, Patman once asked Federal Reserve Chair Arthur Burns, "Can you give me any reason why you should not be in the penitentiary?"  
<https://www.theatlantic.com/politics/archive/2016/10/how-democrats-killed-their-populist-soul/504710/>

The institutional reform faction of the Democratic Party immediately replaced Patman with the committee's 4<sup>th</sup> ranking member, Henry Reuss (D-WI).<sup>15</sup> While Reuss expressed a seemingly genuine commitment to financial reform, he was also a strategic political actor who recognized the changing power dynamics within the congressional party. Soon after assuming his new position, Reuss candidly and colorfully explained, with a gesture towards the empowered reform caucus and the party leadership, "from now on, the sword of Damocles will be hanging over every chairman (Zelizer 2004, p.168)."

At the same time Reuss was elected to the chairmanship of the House Banking Committee, a parallel development occurred in the Senate, as William Proxmire (D-WI), another Wisconsinite, replaced Sparkman (D-AL) as chair. As Proxmire warned upon his ascension to the chairmanship, "The banking industry was too comfortable with Sparkman and Robertson and Fulbright—a long succession of Southern chairmen."<sup>16</sup>

The new northern Banking Committee chairs shared an understanding of regulation and market competition that was increasingly common among Democrats and liberal economists, and distinct from their southern populist predecessors. While John Sparkman and (especially) Wright Patman warned that eliminating the New Deal regulatory regime would pave the way for a national banking monopoly, Reuss and Proxmire argued that repealing "artificial" constraints would disrupt local monopolies to the advantage of savers and borrowers.

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<sup>15</sup> After serving as committee chair for over a decade, Patman would awkwardly serve his 23<sup>rd</sup> and final term in Congress under Reuss's chairmanship.

<sup>16</sup> Cowan, Edward. Jan 5, 1975. "New Man in the Chair." *New York Times*.

On assuming their respective chairmanships, Proxmire and Reuss heightened the anxieties of industries that benefited from the New Deal regulatory regime, by asserting that the end of southern rule marked the discontinuation of business as usual. In his first major decision as chair, Reuss commissioned a study of “Financial Institutions and the Nation’s Economy (FINE)” headed by pro-deregulation economists, and scheduled a seven-day hearing focusing on the commission’s findings, which unsurprisingly called for the elimination of Regulation Q, expansion of NOW accounts, and the deregulation of bank assets.<sup>17</sup>

The FINE hearings made the problems with the New Deal regulatory regime for finance salient, and set the agenda for the House and Senate Banking Committees work over the next several years, but they did not produce immediate results. In 1975, a bill that would have permitted NOW accounts nationwide was defeated on the House floor. In 1976, Reuss failed to move a deregulation bill out of committee. Reuss lamented, “a majority of the committee is not yet ready for a comprehensive reform bill that tries to do something for consumers.”<sup>18</sup>

Despite his efforts, Reuss failed to achieve even modest deregulatory reform during the 94<sup>th</sup> Congress (1975-76). While Reuss maintained his ideological preference for more large-scale deregulation, these failures dampened his faith that it was politically possible.

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<sup>17</sup> James Pierce, Consultant and Director of the FINE Study, House FINE Hearings.

<sup>18</sup> Lyons, Richard. May 4<sup>th</sup>, 1976. House Unit Shelves Bill to Increase Bank Competition. *Los Angeles Times*.

In an apparent dig at Ralph Nader, Reuss continued, “Consumers didn’t make their voices heard.” In response, Nader blamed Reuss “weak leadership,” and offer the unsolicited advice that “you have to run an operation like this like a top sergeant: mobilize, get a bill with broad-based support, one that people can understand, get material out to the media.”

However, the Carter Administration clearly read the legislative politics differently. On June 9<sup>th</sup>, 1977, Treasury Secretary Michael Blumenthal forwarded a deregulatory proposal to the House Banking Committee that was significantly more ambitious than anything Reuss or Proxmire had seriously considered in their respective committees. The Administration's bill proposed expanding NOW nationwide, narrowing the scope of the Regulation Q interest rate ceilings and lowering reserving requirements. Carter's bill also included new mechanisms to expand membership in the Federal Reserve System (FRS)—most notably, by having the Treasury pay commercial banks interests on the reserves they are required to hold as members of the FRS.<sup>19</sup>

The thrust for upending the New Deal regulatory regime in finance came from the very top of the Democratic Party, and was motivated by a vision of the party's collective interest. President Carter insisted that major deregulation was essential, and emphasized that the Regulation Q interest rate ceiling was “particularly unconscionable” during a period of hyperinflation.<sup>20</sup> For Carter and his economic team, Regulation Q and other New Deal financial regulations chiefly functioned as anti-competitive protections that granted local monopolies to depository institutions at the expense of the diffuse interests of American savers and consumers. As his chief domestic policy advisor noted, “President Carter, *initially almost alone*, recognized that if the Democratic party was to retain the loyalty of the American people and remain the majority party at the presidential

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<sup>19</sup> Congressional Archives, 96<sup>th</sup> Congress, Records of the Senate Committee on Banking: Membership in Federal Reserve 1977-80, Box 46. The document in title “Comparison of S.1664, S.1668, and S.1873 (Dated July 19<sup>th</sup>, 1977).

<sup>20</sup> Sinclair, Ward. Nov 23<sup>rd</sup>, 1979. The Battle for Big Bucks: Contrasting Banking Deregulation Bills Bring Immense Pressure on Congress. *The Washington Post*.

level during a conservative period, it needed to move into a post-New Deal era while still retaining the best of the party's traditions (Eizenstat 1994, p.3, emphasis added)."

By coupling financial deregulation and monetary control within the same bill, the Carter Administration employed a two-prong approach to the national crisis of hyperinflation. On the one hand, financial deregulation would ease the pain of inflation (and the corresponding credit crunch) by enabling American savers to receive a higher return on their deposits, and lower reserve requirements would allow banks to lend a larger share of their cash, and thereby expand access credit. Meanwhile, the Administration hoped that the Federal Reserve could curb inflation if more banks joined the FRS.

While Fed membership included several perks, reserve requirements became increasingly costly for banks during the period of persistent inflation—the depreciation of funds in savings accounts incentivizes businesses and consumers to spend more while saving less. But the same inflationary pressures that made Fed membership more costly for banks also intensified the Federal Reserve's ambition to include more banks in the FRS. The Federal Reserve believed that systematic increases in interest rates were required to curb inflation, and the Fed's ability to systematically increase interest rates required expanding membership in the FRS.

In a joint letter to Treasury Secretary Blumenthal, Reuss and St. Germain expressed serious reservations about the policy and politics of the Administration's bill. First, the leaders of the House Banking Committee suggested that the proposal was inappropriately expansive, asserting that while all of the measures included in the package "deal with substantial financial issues, we are not convinced that they are clearly interrelated."

Second, they expressed deep concern about the politics of paying banks for reserves: “Clearly, the payment of interest on reserves would be costly and could be regarded as a bonanza for the big banks.” Third, Reuss and St. Germain reference the failure to enact more modest deregulatory reform in 1975, after the FINE Report hearings, and question whether by “tying the NOW account issues to the membership in the Federal Reserve System issue, we will be in a position to present a more compelling argument to the full House than was the case two years ago.”<sup>21</sup>

Reuss’s counterpart in the Senate felt similarly. In his own letters to Secretary Blumenthal, Proxmire asserted, “I believe NOW accounts and the issue of Federal Reserve membership to separable.”<sup>22</sup>

Proxmire and Reuss agreed that coupling financial deregulation and monetary control was a political nonstarter. However, they disagreed on which set of policies to prioritize. Proxmire was a fervent advocate for financial deregulation, but he was skeptical that curbing inflation required expanding Federal Reserve membership. Interestingly, the renowned libertarian economist Milton Friedman, whose advice Proxmire sought, may have informed Proxmire’s views. A detailed letter from Friedman to Proxmire began, “I do not believe that a decline in Federal Reserve membership threatens the conduct of monetary policy or control of the monetary aggregates. Neither

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<sup>21</sup> Congressional Archives, 96<sup>th</sup> Congress, Records of the Senate Committee on Banking: Membership in Federal Reserve 1977-80, Box 46. Letter from Henry Reuss and Fernand St. Germain to Treasury Secretary Michael Blumenthal (Date July 16<sup>th</sup>, 1977).

<sup>22</sup> Congressional Archives, 96<sup>th</sup> Congress, Records of the Senate Committee on Banking: Membership in Federal Reserve 1977-80, Box 46. Letter from William Proxmire to Treasury Secretary Michael Blumenthal (Date July 21st, 1977).

does the erosion of the membership threaten the safety and soundness of the banking system.”<sup>23</sup>

On the other hand, by the beginning of the 96<sup>th</sup> Congress, Reuss was intent on solving the Fed membership problem, but did not anticipate fundamentally restructuring the banking industry by dismantling the New Deal regulatory regime during the session. Ironically, at the start of the session, Reuss insisted, “We don’t have the heavy legislative workload we had in the last Congress, but we do have one matter of primary importance and that is the Monetary Control Act of 1979, which I have just put into the hopper.”<sup>24</sup>

Unlike the initial bill proposed by the Carter Administration, Reuss’s Monetary Control bill would impose mandatory reserve requirement on all national banks, regardless of their Fed membership status, thereby eliminating the main motivation banks had for opting out of the FRS. Reuss urgently wanted to solve the membership problem, but he was reluctant to provide banks with the generous windfall of interest payments on reserves, at the expense of taxpayers.

In May, after several failed attempts at moving his preferred bill out of committee, Reuss hashed out a compromise bill with William Moorhead (D-PA) and the House Banking Committee’s most conservative Democrat, Doug Barnard (D-GA), which effectively lowered the share of funds banks would need to hold on reserve by excluding funds in savings accounts from the calculation.<sup>25</sup> Moreover, the compromise bill would only impose mandatory reserve requirements on the nation’s largest commercial banks.

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<sup>23</sup> 95<sup>th</sup> Congress, Senate Committee on Banking, Federal Reserve Membership, Box 46. Letter from Milton Friedman to Senator Proxmire (Dated August 21<sup>st</sup>, 1978).

<sup>24</sup> Farnsworth, Clyde. Feb 8, 1979. Talking Business: with Reuss of House Banking Committee. *New York Times*.

<sup>25</sup> *Baltimore Sun*. May 23<sup>th</sup>, 1979. Reuss Unveils Compromise on Fed Exodus; Wall Street Journal. Jun 6<sup>th</sup>, 1979. Measure to Stem Exodus of Banks from Fed Gains.

On June 5<sup>th</sup>, 1979, the House Banking Committee approved the revised bill by a vote of 26-14.<sup>26</sup> In late July 1979, the House easily passed the compromise Monetary Control Bill, which had been amended to expand the use of NOW accounts, on a 340 to 20 vote.<sup>27</sup>

Under Proxmire's leadership, the Senate responded to H.R. 7 by passing a considerably more ambitious deregulatory reform bill—including the elimination of Regulation Q, among other major deregulatory reforms—that omitted monetary control measures. Then, in a “sort of legislative chicken game,” Proxmire refused to advance a monetary control bill that did not include the elimination of Regulation Q, even as Reuss and St. Germain maintained that they could not get a bill that eliminated Regulation Q through the House.<sup>28</sup>

In the pre-institutional reform House of Representatives, the prospects for financial deregulation and monetary control would have likely died at this point, or, at most, Reuss may have managed to advance a much less ambitious deregulatory bill that did not include monetary control. However, in the institutionally reformed Congress, President Carter and Chairman Reuss were able to summon the support of an empowered Democratic Party leadership in the House.

Despite his personal ideological inclinations and close ties to organized labor, Speaker Tip O'Neill was reliably committed to President Carter's deregulation agenda.<sup>29</sup>

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<sup>26</sup> *Los Angeles Times*. House Unit Oks Bills to Help Stem Exodus from Fed. Jun 6<sup>th</sup>, 1979.

<sup>27</sup> *Wall Street Journal*. Jul 23, 1979. House Easily Approves Compromise Bill to Reduce the Exodus of Banks From Fed.

<sup>28</sup> *Hartford Courant*. Nov 25, 1979. House, Senate Split Over Deregulation of Banking.

<sup>29</sup> Rattner, Steven. Aug. 7<sup>th</sup>, 1977. In the Senate, Carter Won't Have a Commander Like Tip O'Neill. *The New York Times*.



O'Neill had previously advocated for price controls as a policy tool to fight inflation, but as the Democratic Party leader in the House, he sought to promote his party's brand by unifying with the Democratic president, and using his institutional powers to advance general purpose legislation that could provide immediate benefits to American savers and consumers. For example, when Elliot Levitas (D-GA) held up airline deregulation in the House Aviation Subcommittee—likely because Delta Airlines was headquartered in his district—Carter turned to Speaker O'Neill who successfully intervened (Crain 2007). But Tip O'Neill's power to advance President Carter's deregulatory agenda extended far beyond persuasion.

The institutional reforms of the mid-1970s gave the Speaker of the House the power to select Democrats—who constituted a lopsided majority—on the Rules Committee. Tip O'Neill was the first House Speaker to begin seriously exploiting this newfound power (Rohde 1991), and he did so to advance Carter's deregulatory agenda. For example, Douglas Arnold (1990) describes how O'Neill used his authority over Rules to pass Carter's massive energy deregulation bill in 1977:

“Speaker O'Neill invented and adapted several procedural rules that helped the reform coalition to stick together and that provided further political insulation for legislators...From the very beginning he insisted that the House act on the National Energy Plan as a single package...The Speaker then persuaded the House Rules Committee to send the entire energy package to the floor under a modified closed rule (p.255).”

O'Neill's powers were further enhanced by the 96<sup>th</sup> Congress, when Richard Bolling, a savvy student of legislative procedure and close “personal ally and friend” of

Tip O'Neill, became chairman of the Rules Committee (Rohde 1991, p.99). Under O'Neill's command, Bolling greatly accelerated the unorthodox use of closed and special rules to enact legislation. Such was the case with H.R. 4986, the Depository Institutions Deregulation and Monetary Control Act of 1980.

As it remained clear the Reuss could not pass a bill that eliminated Regulation Q in the House Banking Committee, the Democratic Party leadership used a series of procedural tactics to circumvent the committee and construct an ambitious deregulatory reform bill that could pass on the House floor. In late February of 1980, Democratic leaders established a joint conference committee to hash out an omnibus bill. O'Neill selected Reuss and the most relevant subcommittee chairs, St. Germain who strongly supported deregulation and Annunzio who strongly opposed it. For his final selection, O'Neill bypassed 21 more senior Democrats to appoint the House Banking Committee's most fervent deregulatory reformer, the freshman Doug Barnard (D-GA). In the post-reform House, Speaker O'Neill was unconstrained by seniority, and able to ensure that the House team of conferees maintained a strong deregulatory leaning, consistent with the Democratic President.<sup>30</sup>

Moreover, in the weeks preceding the joint conference committee, Democratic leaders in both chambers avoided what, at the time, was the standard procedure of documenting guidelines for the conferees. As Congressional Quarterly noted, the "House and Senate Banking conferees" were working on "an omnibus banking bill...without clear-cut mandates from their committees." Indeed, even though the two chambers passed

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<sup>30</sup> Rybicki, Elizabeth. 2019. "Resolving Legislative Differences in Congress: Conference Committees and Amendments Between the Houses." Congressional Research Service.

remarkably disparate bills, “neither committee marked up alternative legislation, and neither took consensus votes on the issues in conflict.” The Congressional Quarterly Weekly Report asserted that the gambit of forming a conference committee to hammer out a compromise between two radically distinct bills was unusual and would likely “portend as a tough a conference” as earlier failed rounds that “ended in stalemate.”<sup>31</sup> On the contrary, by removing the opportunity for the House Banking Committee majority to signal its preferences, which almost certainly would have omitted Regulation Q repeal and other deregulatory reforms, party leaders increased the discretion of the conferees.

To seemingly everyone’s surprise, the joint committee produced an omnibus bill that included all of the major deregulatory provisions in the Senate bill. However, this bill clearly violated a House rule that required joint conference committee reports to exclusively include provisions that were germane to a corresponding bill that had already passed in the House—indeed, seven of the nine titles of the bill (all deregulating aspects of the financial industry) had never even passed in the House Banking Committee, let alone the full chamber. To advance the joint conference report to the House floor for a vote, the Rules Committee passed a special rule waiving the germaneness requirement.

The special rule for the conference report also waived a House rule that allowed members to request a vote on individual Senate amendments included in the conference report that were not already enacted in an earlier House bill. Without this waiver, the House Rules Committee would have had to schedule votes on any such amendments

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<sup>31</sup> The report quotes staffers from the House and Senate committees who were equally pessimistic on the prospects of a compromise bill. “‘It’s going to be a difficult conference,’ sighed one Senate aide. And a House committee staffer questions the conferees’ ability to complete a compromise by [the] March 31 [deadline].” Gregg, Gail. 1980. “Conferees to Resume Work on Omnibus Banking Bill.” *Congressional Quarterly Weekly Report*.

before the conference report, in its entirety, went to the floor for vote. Presumably, this rule was waived because opponents of deregulation requested such votes, and if recent history were a reliable indicator, some of these key provisions (such as the Regulation Q repeal) would likely have been struck from the House conference report.

Finally, Democratic leadership also employed tactics to ensure that most Democratic (and Republican) legislators were truly ignorant to the enormous economic consequences of this complex bill on highly esoteric regulatory matters, and largely insulated from interest group lobbying. The House voted on the conference report two business days after it was released, and the bill summary neglected the Regulation Q repeal, as well as state usury preemption, which was the second most highly controversial provision of the bill.

Opponents and supporters alike acknowledged the unorthodox process Democratic leaders used to enact DIDMCA. A spokesperson from Ralph Nader's Public Interest Research Group complained, "It's an incredible way to legislate." Another critic lamented, "People didn't know what they were voting on."<sup>32</sup> Indeed, Frank Annunzio (D-IL)—a protégé of Wright Patman and chair of the House Subcommittee on Consumer Affairs—was so upset by the untraditional process that he stormed out of the conference room without signing the joint report.<sup>33</sup> Most strikingly, speaking on the House floor for the Rules Committee, Joe Moakley (D-MA) introduced the special rule by acknowledge that "it is unfortunate that the House did not originally have an opportunity to consider all the provisions that are now in this conference report."

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<sup>32</sup> Babcock, Charles. Apr. 15<sup>th</sup>, 1980. The Banking 'Reform' Bill: Parceling Out the Goodies. *The Washington Post*.

<sup>33</sup> Babcock, Charles. Apr. 15<sup>th</sup>, 1980. The Banking 'Reform' Bill: Parceling Out the Goodies. *The Washington Post*.

While the use of special rules and tactics to circumvent policy committees became common in the ensuing decades, the techniques discussed above represented procedural innovations by party leaders who were expanding their powers in a post-reform House in which the Rules Committee increasingly functioned as the arm of the Speaker (Rohde 1991; Sinclair 1984).

As a result of the elimination of the seniority rule at the beginning of the 94<sup>th</sup> Congress (1975), a pro-deregulation policy entrepreneur, rather than a traditional labor-liberal or southern populist, chaired the House Banking Committee. However, the collective policy entrepreneurship of Henry Reuss and William Proxmire was insufficient to enact even modest financial deregulation. Rather, an increasingly powerful Democratic Party leadership—including President Carter, Speaker O’Neill, and House Rules Committee Chairman Richard Bolling—was the driving force behind the party’s turn against the New Deal regulatory regime in finance.

### **Diminished Parochialism in Democrats’ Voting on Financial Regulation**

In addition to reshaping the House Committee on Banking and Currency, and empowering party leadership to employ tactics detailed above, I theorize that congressional reforms also reoriented rank-and-file members away from their constituent-centered orientation in favor of leadership and the party’s perceived collective interests.

I test the effects of congressional reform on the move away from constituent-centeredness by measuring the relationship between district factors and legislative behavior on financial regulation. I combine state and district-level economic and demographic data with an original dataset of members’ voting behavior on financial and

banking regulatory bills that structure competition and the concentration of economic power. More specifically, these bills addressed regulations on at least one of the following issues: interest rates on deposits (and the differential between S&Ls and commercial banks), interest rates on loans, NOW accounts, intra and interstate bank branching, and bank holding companies. I identified 34 roll calls on such votes held in the House during this period, within nine distinct congressional sessions from the 81<sup>st</sup> (1949-50) to the 102<sup>nd</sup> (1991-92) Congress.

I coded each relevant House bill as either increasing or decreasing the overall level of economic regulation. For each roll call, I assigned a member a 0 if they casted a pro-regulatory vote, a 1 if they took an anti-regulatory vote, and dropped them if they abstained or were absent.<sup>34</sup>

For each House Democrat who served during a Congress in which a significant financial regulatory bill reached the floor, I use the average of these scores as an indicator of their legislator behavior on financial deregulation in that particular Congress. A positive 1 indicates that a member voted yes on every bill that would retrench New Deal financial regulations, and voted no on every bill that would preserve or expand such regulations. A zero indicates the opposite.

Using the beginning of the 94<sup>th</sup> Congress (1975) to demarcate the pre- and post-congressional reform eras, I ran two multivariate regression models on Democratic legislators. In the first model I pool Democrats from the 81<sup>st</sup> to 93<sup>rd</sup> Congress. In the

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Pro-regulatory votes are yes votes on bills that would yield an overall expansion of financial regulation, or no votes on bills that would retrench financial regulations. Anti-regulatory votes are yes votes bills that would decrease financial regulation, and no votes and bills that would increase regulation.

second model I pool Democrats from the 94<sup>th</sup> to the 102<sup>nd</sup> Congress. I include time dummy variables to control for the distinct agenda items in each Congress.

A difficulty in interpreting quantitative measures based on roll call voting across Congresses is that such scores are not comparable if the ideological substance of the agenda is relatively static, which is often not the case, and this was certainly not the case with regards to financial and banking regulation during this period. Nevertheless, these deregulatory scores provide a reliable measure of the relative position of Democrats within a congressional era. What we are interested in is a comparison of the predictive power of district-level economic and demographic variables on the relative position of Democrats on financial regulation (i.e. *deregulation score*) across periods.

For predictive variables, I include measures of district-level demographic and industry variables helpfully compiled and shared by Scott Adler, most of which come from the Census. These include the number of blue-collar workers, construction workers, African Americans, and the number of residents living in urban and in rural farm areas. I also use data from the Federal Deposit Insurance Corporation (FDIC) to construct a measure of banking concentration by state. Specifically, I divide the total bank deposits by the number of banks as a proxy of banking concentration within the state—larger numbers indicate larger banks.

For the most part, each of these variables is intended to represent an interest or identity group that the New Deal regulatory regime materially benefited or harmed. Most importantly, if member were more parochial prior to the congressional reform of the mid-to late-1970s, we should expect to see that members from districts with a larger share of union members and blue-collar workers—who benefitted from regulations the buttressed

local S&Ls and commercial banks, and thereby promoted local homebuilding and business construction—were less likely to cast anti-regulatory votes against the New Deal regulatory regime.

To test the effect of ideological change, I also include 1<sup>st</sup> dimension DW-Nominate scores and, in the post-reform model, a dummy variable for Democrats who entered Congress in the aftermath of Watergate (1975-1979).

The results are presented in Table 1. As expected, Democrats from states with a more concentrated banking industry were more likely to vote for deregulation, while Democrats from states with smaller banks were more likely to cast votes that maintained the New Deal financial regulations. This was true before and after the congressional reforms of the mid-1970s, but that is where the similarity between these eras ends.

Table 1: Effects of District-Level Group Variables on Democrats' Deregulation Scores

	Pre-Reform (1950-1974)	Post-Reform (1975-1992)
Bank Size	.40*** (.11)	.46** (.16)
Blue Collar	-2.52*** (.52)	.97 (.05)
Construction	.02 (.51)	-2.47 (2.36)
Urban	.33*** (.09)	-.09 (.09)
Rural Farm	.85*** (.18)	-.81* (.41)
Black	.30* (.14)	-.016 (.08)
DW-Nominate	-4.84 (5.33)	-2.77 (4.19)
Watergate Baby Cohort		.97 (1.4)
Dummy (84 <sup>th</sup> /95 <sup>th</sup> )	-14.5*** (2.77)	-10.9*** (2.08)
Dummy (89 <sup>th</sup> /96 <sup>th</sup> )	53.3*** (2.74)	4.5* (2.1)
Dummy (90 <sup>th</sup> /97 <sup>th</sup> )	83.1***	26.5***



	(3.0)	(2.4)
Dummy (91 <sup>st</sup> /101 <sup>st</sup> )	-3.3	-17.7***
	(3.0)	(2.5)
Dummy (93 <sup>rd</sup> /102 <sup>nd</sup> )	17.6***	4.14
	(3.2)	(2.5)
Intercept	10.9***	50.2
	(2.9)	
Adjusted R <sup>2</sup>	.58	.22
N	1,374	1,773
Floor Votes	8	26

\* p < .05, \*\* p < .01, \*\*\* p < .001

As Table 1 reveals, district factors are much stronger predictors of Democrats' voting behavior on the New Deal regulatory regime for finance before the congressional reforms of the mid-1970s. Democrats from district with more blue-collar workers—a proxy for union membership—were significantly less likely to cast deregulatory votes in the pre-reform Congress. After congressional reform in 1975, blue-collar employment (and presumably union membership) does not predict Democrats' deregulation scores. Similarly, the share of constituents who live in urban areas and are African-American corresponds to more deregulatory vote behavior prior to reform, but these variables are weakly correlated after reform. The greater predictive power of constituent factors on deregulatory scores is summarized by fact that the independent variables in the pre-reform model explain about three-fifths (.58) of the variation in Democrats' voting, but just over one-fifth (.22) in the post-reform era.

These findings are entirely consistent with my theory that institutional reforms during the mid-1970s increased the likelihood that Democrats would support deregulatory bills that deeply antagonized powerful constituent groups. As Democratic Party leadership consolidated power in the House, rank-and-file Democrats had a greater incentive to toe the party line, by supporting reforms that provided diffuse benefits to

American consumers and savers, which Democratic Presidents and Speakers thought would improve the party's collective interest in maintaining control of government.

Democrats with more conservative DW-Nominate scores, and Watergate Baby Democrats, were virtually indistinguishable in their support for financial deregulation in the post-reform Congress. This suggests that the insurgence of the Watergate Babies as an ideological faction within the Democratic Party, and ideological change more generally, do not explain why Democrats upended the New Deal regulatory regime.

## **Conclusion**

The New Deal regulatory regime for finance was created and perpetuated within an institutional context that encouraged congressional Democrats to be constituent-centered, and to empower southern populist committee chairs. In this context, the caucus as a whole was especially responsive to the demands of small local banks and S&Ls—and allied industry groups and labor unions—that were situated across many districts and states. In these decentralized Congresses, Democratic Party leaders were unable address national concerns about market efficiency and consumer interests, since deregulatory reforms threatened the local banks, S&Ls, realtors, construction firms and laborers who benefitted from New Deal financial regulations.

During the 1970s, these entrenched interests continued to defend the key provisions of the New Deal regulatory regime, but Democrats became less responsive to their demands. In the new institutional context of the 1970s, a more centralized Democratic Party leadership used its new powers over the legislative process to enact deregulatory reforms that could not pass through the normal order. Furthermore, by shifting the incentive structure for rank-and-file members, the congressional reforms of

the 1970s made it more likely that rank-and-file Democrats would support bills that served the diffuse interests of American consumer-savers, despite fierce opposition from the entrenched constituent groups.

However, given the economic consequences of Democrats' deregulatory turn, the upshot of these findings is not a simple success story about Responsible Party Government in the U.S. Congress.

While prominent critics lament about the pathologies of Congress's parochialism (Howell and Moe 2016) and weak party government (APSA Report 1950; Rosenbluth and Shapiro 2018), this article complicates the normative case for centralized power in Congress. The New Deal regulatory regime in finance did not merely buttress small local banks and S&Ls at the expense of Americans looking for access to mortgage credit and the higher rates of return offered by securities markets. New Deal financial regulations, while inefficient, created employment opportunities in every congressional district and promoted remarkably even economic development throughout the nation. Moreover, by protecting this decentralized economic system of small local banks and firms, the New Deal regulatory regime preserved an army of countervailing interests that used its economic and political might to constrain Wall Street and financial markets, and substantially mitigate the concentration of economic and political power. As Louis Brandeis and his disciples (including Wright Patman) would have predicted, by eliminating protections for small local "monopolies," and unleashing financial markets on the broader economy, Democrats betrayal of the New Deal regulatory regime resulted in (inter)national monopolization, and unprecedented levels of wealth inequality between individuals and across geographic regions of the nation (Brandeis 2009).

Furthermore, although stronger national parties sometimes compete for power by championing policies that address important national problems and provide diffuse public benefits, they also compete by raising and spending huge sums of money. As interparty competition for control of government intensified, the more centralized Democratic Party in Congress built a national fundraising infrastructure (Kolodny 1998). Meanwhile, as financial deregulation increased the disposable wealth of Wall Street financiers and large investors, their disposable wealth fueled the Democratic Party's national campaign infrastructure. Consequently, Democrats deregulatory pursuits during the 1990s—most importantly the repeal of the prohibition on interstate bank branching in 1994, and the Glass-Steagall firewall between commercial and investment banking in 1999—are better explained by Wall Street donations than the interests of American savers and consumers (Witko et al. 2021; Kelly 2020; Keller and Kelly). Just as the decentralized congressional institutions of the pre-reform era reinforced decentralized American industries, today's more centralized congressional parties complement the concentration of economic power.

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