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The Housing Bailout: Constitutional Infirmities Remain, but a Ray of Hope

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At 9:30 this morning, the President spoke on the continuing negotiations with Congress to pass a plan to address the credit crisis. The gist of his remarks was: If it be done, let it be done quickly. Conservatives must append a further mandate: If it be done, let it be done constitutionally. Constitutionality is not a mere feature of legislation; it is a threshold requirement. All Members of Congress take a pledge to "support and defend the Constitution," and that duty does not fade away in a time of crisis—indeed, it is then especially that constitutional fidelity is most crucial and most endangered.

The secretary of the Treasury's original bailout plan was met with concern by constitutionalists for its shortcomings in adherence to fundamental principle. In particular, the plan was criticized for its inattention to the federal government's enumerated powers, the lack of meaningful standards to cabin the extremely broad grant of discretion to the Treasury secretary (the "nondelegation" problem), limitations on judicial review over the exercise of that discretion, and other separation of powers problems. These failings render the Treasury proposal, and those so far that have built on it, unconstitutional.

Below, we analyze the constitutional aspects of two current proposals to address the credit crisis.

Fundamental Principles. If the bailout is to pass constitutional muster, lawmakers must concern themselves with at least the following specifics, explained in greater detail in our previous *WebMemo*[1] while keeping in mind the broader outlines of its constitutional authority.

- *Type and Scope of Indebtedness.* The type of financial instruments or debt that the Treasury Secretary can purchase, as well as the industries that may seek relief, should be defined by statute carefully so as to limit the secretary's discretion.
- *Standards to Guide the Secretary's Discretion.* Congress must craft legislation that contains an objective set of criteria that would guide the secretary's exercise of discretion in practice and not just in theory. As explained further below, the criteria must be specific enough to distinguish between lawful and unlawful actions.
- *Meaningful Judicial Review.* Citizens adversely affected by the government's actions must be able to seek a redress in the courts for fundamental constitutional violations or damages at law.

These fundamental principles are not met by the "Agreement on Principles" negotiated last night by House and Senate leaders and the White House and wrought into legislative text this morning. Thus, our original analysis of that proposal remains relevant. The new proposal feigns attention to this paramount shortcoming but fails to fix it. The draft legislative text includes a long list of "considerations" that the secretary "shall" consult when exer-

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cising authority under the act. When deciding whether to purchase particular assets from a particular institution, the secretary would have to consider, among other factors, whether the purchase would "provide[] stability or prevent[] disruption to the financial markets or banking system," "help families to keep their homes and stabilize communities," and "ensure[] that as many financial institutions as possible participate in the program, without discrimination…based on their size, geographic operation," and other factors.

Taken altogether, these vague, overlapping, and contradictory "considerations" are both incoherent and empty. They contain no limiting principle to define which acts are lawful and which are not. The long list of "considerations" does more to expand the secretary's possible range of discretion than to define it. Thus, the list does not create a circumscribed delegation of authority but instead preserves a blank check of legislative power turned over to the Treasury secretary. The broad delegation of power to the Treasury secretary therefore remains unconstitutional.

In contrast to a laundry list of considerations that a future secretary could employ to justify anything at all, a constitutional standard would provide objective criteria that define and limit his range of action. For example, a constitutional law might state: "If the secretary finds A, B, and C [which are all objective criteria, and at least one of which is tied to a legitimate government function], he may purchase…" By implication, that language means that if the secretary cannot find those three criteria, his action would be unlawful. That is what the Constitution requires to render a grant of authority under law.

Further, the agreement includes new unbounded delegations to the secretary of the Treasury. In addition to the power to spend up to $700 billion, in total at any time, to purchase assets of any type (the strictures on this grant are loosened from Treasury's initial proposal to include equity investments), the agreement would also direct the secretary to set standards for executive compensation and allow him to exercise the powers that come with equity ownership, including some degree of direct corporate control. To the extent they would permit elimination of compensation for which an executive has a vested contractual right, these provisions raise significant taking and due process concerns.

Though the new proposal does reinstate judicial review, it does so in a way that provides no firm standards to actually constrain the secretary's discretion. The agreement would require that the secretary be "prohibited from acting in an arbitrary or capricious manner." But this standard of review is meaningless, or at best, circular, if the secretary is authorized to do whatever he thinks best. Despite this emptiness, it would still be an invitation to litigation. Lawsuits will be plentiful, injunctions perhaps only somewhat less so. Judges—not the statutory text—will determine the bounds of the authority that the secretary may exercise. Judges, however, cannot logically determine whether an action is arbitrary or capricious when the underlying criteria for making such a determination do not exist—a recipe for judicial arbitrariness and activism. Thus the review provision will sap the vitality of the secretary's mandate while providing no objective criteria to guide his acts. It is, at once, the worst of both worlds.

In lieu of providing clear policy direction, the proposal would instead impose possibly unconstitutional oversight mechanisms. The plan is weighted down with a "strong oversight board," "detailed reports to Congress," an additional, questionably "independent" inspector general, and additional audits by Congress's Government Accountability Office. In this way, the legislative branch—seemingly so reluctant to exercise its policymaking and lawmaking authority—would interfere in the secretary's authority as executor of the law, which is power delegated to him, through the President, in Article II of the Constitution.

In particular, these constitutional breaches suggest bad policy as well. Instead of writing detailed laws that the President is then responsible to exe-

1. Todd F. Gaziano and Andrew M. Grossman, "All Deliberate Speed: Constitutional Fidelity and Prudent Policy Go Hand in Hand in Fixing the Credit Crisis," Heritage Foundation *WebMemo* No. 2079, September 24, 2008, at *http://www.heritage.org/Research/Economy/wm2079.cfm*.

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cute, Congress delegates vast new authority to the executive branch to "fix" the problem *de jure* and then tries to invent new ways to micromanage and nitpick the exercise of the authority. Such a power-*sharing* relationship is the exact opposite of the constitutional separation of powers perfected by the Framers of our Constitution. Ignoring that command abandons a great and durable mechanism of accountability that empowers citizens to punish public officials whose performance is sub par. All that remains is partisan bickering, finger-pointing, and reprisals.

As an example of a proposal that avoids constitutional pitfalls, the Republican Study Committee (RSC) has released an independent plan to address the current economic malaise. Without commenting on the policy merits, we analyze here that plan's constitutional status.

Like the "Agreement on Principles" described above, the RSC proposal exists as a set of "principles" rather than fleshed out legislative text. These principles are very different from those in the leadership/White House proposal. The RSC would expand the federal government's insurance of mortgage-backed securities to cover the entire market, up from half at present. This expansion would be funded by assessing premiums on the holders of those assets. Temporary tax relief provisions, including perhaps a moratorium on the taxation of capital gains, is designed to free capital to circulate in the economy, and a temporary suspension of dividend payments by regulated financial institutions is intended to the same end. Finally, the plan would enact a variety of regulatory changes: revision to the accounting of mortgage-backed securities and reporting requirements regarding them; changes to the mandates of the "government-sponsored enterprises," such as Fannie Mae and Freddie Mac; mandatory audits of the books of failed companies; and requirements that the SEC, Treasury, and the Federal Reserve issue further policy recommendations to Congress no later than January 1, 2009.

Most strikingly, this proposal appears to raise no serious issues of improper delegation. Its mandates are far more modest than those in the leadership/White House proposal, and it seems to spell them out in sufficient detail to pass muster both under the Supreme Court's jurisprudence on delegation and the actual Constitution itself.

Further, there is certainly less question of whether the RSC proposal is *ultra vires*—that is, beyond the powers enumerated in the Constitution—because it requires no new acts of the government. It would primarily expand several existing programs—in size but not in scope—and modify existing regulatory regimes. Its chief component, temporary changes to the tax system, is well within the government's power to tax, and its expansion of government insurance for mortgage-backed securities at least raises no new constitutional issues, especially if it is implemented in a manner similar to the Federal Deposit Insurance Corporation—as a voluntary mechanism.

Due primarily to its specificity, the RSC proposal avoids constitutional pitfalls. This conclusion does not, of course, speak to its economic merits, but it provides an example of the principles necessary to pass constitutional muster.

A Constitutional Duty. The RSC proposal suggests that Congress can put together a plan that does not violate our fundamental law. Those who, for reasons of economic policy, favor the leadership/White House proposal must correct its legal flaws if they seek, in good faith, to uphold their duty to the Constitution and the people. To do otherwise would be to set bad precedent that may stain constitutional practice for generations to come.

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