WebMemo
Published by The Heritage Foundation

No. 2164
December 9, 2008

Auto Bailout Bill: Nationalizing Detroit?

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Would Washington do a better job running the automobile industry than Detroit would? Taxpayers may be about to find out. Under legislation proposed yesterday by congressional leaders, Detroit-based automakers would be offered some $15 billion in federal low-interest loans. In return, they would be subject to unprecedented federal controls on how they run their businesses.

This is a deal that would serve neither Detroit nor America's taxpayers. Detroit needs to change to respond to the 21st-century marketplace. This plan will instead simply make Detroit more responsive to Washington's politicians. That is the wrong road for the auto industry, and taxpayers, to go down.

Rough Road for Automakers. The Detroit automakers—General Motors, Ford, and Chrysler—have certainly traveled a rough road over the past several weeks. Facing falling sales and bleeding red ink, the chief executive officers of the trio came to Congress last month to ask for as much as $50 billion in federal aid.[1] Their requests, however, did not meet with much sympathy either among the public or among Members. The CEOs were sent back home to Michigan and told not to come back until they had plans for restructuring their troubled enterprises.

Last week, they returned, plans in hand, to renew their request for aid. Again, they received a mixed reception, with few Members willing to write a blank check to the carmakers on the mere promise that they would implement the reforms proposed. The result was the compromise plan announced today: $15 billion in low-interest loans, but only in return for turning substantial control of their corporations over to the government.

Bailout by Invitation Only. Eligibility for the program is limited to firms that submitted restructuring plans to Congress on December 2—thus limiting participation to General Motors, Ford, and Chrysler, since they were the only firms asked to submit such plans.

Aid would be provided in two stages: an immediate bridge loan to forestall possible bankruptcies, and longer-term aid, with repayment over at least seven years. Nevertheless, at current loss rates, the $15 billion would not last long, keeping General Motors and Chrysler afloat only a few months, meaning further funding would likely soon be needed to continue the program.

The program would be overseen by an individual to be designated by the President. This so-called "car czar" would authorize disbursement of money, determine how much goes to each firm, and establish measures for assessing automakers' progress toward restructuring. This czar would also have extraordinary powers over participating firms, with approval authority over all corporate expenditures over $25 million.

This paper, in its entirety, can be found at:
www.heritage.org/Research/Economy/wm2164.cfm

Produced by the Thomas A. Roe Institute
for Economic Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 • heritage.org

Long-Term Restructuring. In addition, the car czar would facilitate the development of long-term restructuring plans for each firm and convene negotiations with representatives of "all interested parties," including unions, suppliers, dealers, and shareholders. If no agreement is reached, Congress itself, according to the legislation, would step in to impose its own restructuring plan on the firm.

The legislation also imposes a raft of specific conditions on automakers. Some track conditions imposed in other recent bailouts: Washington would receive warrants for the purchase of stock in the companies, dividends would be suspended, and executive compensation would be limited.

Other provisions are unique to this bailout, and unusual in their specificity. To no one's surprise, the ownership of corporate jets is banned. More worrisome, the carmakers are required to consider conversion of SUV manufacturing plants to mass transit vehicle production. The bill would also limit the carmakers' ability to fight further regulation, banning them from pursuing court challenges to state laws regarding greenhouse gas emissions.

Politicians Doubling as CEOs. Detroit's automakers need to change, and in a fundamental way. Merely handing over cash to the three firms, as some originally proposed, would simply extend current problems, not resolve them. For that reason, policymakers were correct in rejecting calls for largely unconditioned aid for the automakers.

But micromanagement of the auto industry by politicians and bureaucrats is equally unlikely to achieve the restructuring that is needed. Whatever Detroit's failings, it is unlikely that Washington will be any better at knowing how to run a successful enterprise. Instead, the result will likely be a politically driven restructuring of the industry that is more focused on pleasing electoral constituencies than making products that consumers will buy.

A far better approach to restructuring would be the bankruptcy process, which not only provides the legal means to cancel debt and lower costs but also provides a fair, orderly, and non-political process for making the painful decisions that need to be made.

Congress should reject a bailout of Detroit—with or without strings attached.

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1. See James Gattuso and Nicolas Loris, "The Detroit Bailout: Unsafe at Any Cost," Heritage Foundation *WebMemo* No. 2133, November 16, 2008, at *http://www.heritage.org/research/economy/wm2133.cfm.*