



A progressive political agenda calls for public banking and finance institutions (PBFIs) to be widespread and large enough to meet the challenges of catastrophic climate change, economic exploitation, racial exclusion, and sustainable economic development. To fully succeed, we need the federal government and the Federal Reserve to underwrite PBFIs to the same extent they have supported private finance over the last several decades. Drawing on recent activist efforts and proposals, we describe models that move us toward these goals.

Are Bankers Essential Workers?

Gerald Epstein and
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During the global financial crisis (GFC, 2007–2009), Lloyd Blankfein, CEO of Goldman Sachs, famously said that it was unfair that people were so mad at him and other bankers for crashing the economy because, contrary to common belief, they were doing “God’s work.”¹

God’s work? Maybe so. But they were certainly not doing work for the economy, the taxpayers, or the people. Rather, it turns out, we were all working for them.

1 Daily Mail Reporter, “Goldman Sachs chief says ‘we do God’s work’ as he defends the bank’s mega profits,” *Daily Mail*, November 8, 2009, dailymail.co.uk/news/article-1226114/Goldman-Sachs-chief-says-Gods-work-defends-banks-bumper-profits.html.

However preposterous Blankfein's claim was, he went on to argue something that is contained in almost every *Money and Banking* textbook and that is constantly repeated by economists, politicians, and bankers: "We're very important. We [bankers] help companies to grow by helping them to raise capital. Companies that grow create wealth. This, in turn, allows people to have jobs that create more growth and more wealth. We have a social purpose."

In other words: "Bankers are essential workers."

But the people are not buying it. When they clapped every night on their balconies at 7 p.m. or made signs or sent out heartfelt messages thanking "our essential workers," they mentioned health care workers, first responders, teachers, grocery store workers, delivery people, and farmers, among others. But bankers?

Still, the hard truth is that bankers make themselves "essential" by inserting themselves into the heart of the economy. This becomes most obvious during economic crises. In the run-up to periodic financial meltdowns, bankers' reach, wealth, and power means they can direct the nation's credit and, more important, its human and natural resources in socially perverse and destructive ways. Then, when their reckless actions get out of hand, they threaten all of us with economic destruction, unless we prop them up and bail them out. In this way, bankers and financiers make themselves essential workers the same way the local shake-down artist extracts protection money: pay up, or watch your store burn to the ground.

Believe it or not, the problem gets even worse — policymakers help to make the bankers "essential workers." In the current economic crisis, for example, the Federal Reserve (Fed) and the US Treasury made bankers essential workers to channel funds to small businesses and households and manage the Fed's securities market operations. These private banks stand to earn more than \$17 billion in fees from this work, though they appear poorly

positioned to handle this efficiently and quickly.² For instance, the \$1.7 trillion asset management firm BlackRock has been commissioned by the Fed to manage several of its new bailout funds.³ Bankers stand to gain millions in fees for an activity that could be carried out by the Fed itself just as easily, more cheaply, and without conflict of interest.

Thus, bankers have made themselves essential workers the way that most rent grabbers and middlemen do it: through political power, manipulation, and blocking the competition. These bankers' biggest fear is that public banking would provide this effective competition, nullifying their claims to be essential and therefore worthy of the public's largesse.

All this notwithstanding, there is a real kernel of truth to the bankers' and economists' claims. In any modern economy, especially capitalist ones, money and credit are foundational. They provide key mechanisms through which economic activity takes place, and they are the medium through which everyday transactions occur. They provide a conduit for economic policy. And, perhaps most important, in market-based economies, money and credit provide a key fulcrum on which major economic transformations can be effectuated.

Progressives need to grab this essential mechanism and turn it over to communities and the citizenry, so that they can apply it to their own purposes, rather than allowing bankers to make themselves essential even as they threaten to undermine the

2 Laura Sullivan, "Banks Rake in \$17 Billion in Fees for Small Business Relief Program," *NPR*, May 5, 2020 (Accessed July 8, 2020), [npr.org/2020/05/05/850964030/banks-rake-in-17-billion-in-fees-for-small-business-relief-program](https://www.npr.org/2020/05/05/850964030/banks-rake-in-17-billion-in-fees-for-small-business-relief-program).

3 Pedro Nicolaci da Costa, "A Glaring New Conflict of Interest Undermines Public Trust in Federal Reserve," *Forbes*, April 20, 2020, [forbes.com/sites/pedroacosta/2020/04/20/a-glaring-new-conflict-of-interest-undermines-public-trust-in-federal-reserve/#531d7933135d](https://www.forbes.com/sites/pedroacosta/2020/04/20/a-glaring-new-conflict-of-interest-undermines-public-trust-in-federal-reserve/#531d7933135d).

economy. We also need to design effective ways to help workers, communities, and the public at large to take more control over this critical financial system and use it as a tool for social, environmental, and political transformation.

Thankfully, this is not news to progressive activists and reformers. Many excellent ideas have been developed and promulgated in the United States and abroad to transform the financial system from a den of parasites to a set of useful institutions. Some of these ideas draw on institutions prevalent in other countries, while others are truly homegrown. In fact, there is a long history of successful and crucial public-oriented financial institutions. Ever since the financial crisis of 2007–2009, there has been a resurgence of activism by progressives who are trying to implement and promote socially oriented financial institutions in the United States and abroad.

In this essay, we describe what a socially useful and transformative financial system would look like and what role socially oriented financial institutions could play in that system. The United States and the global economy face many critical challenges, but this essay focuses on four especially important ones: revival and reconstruction of the economy amid the COVID-19 pandemic; transitioning to a carbon-free energy system to avoid catastrophic climate change; addressing racial inequality, poverty, and exploitation; and creating an economy that can produce meaningful and productive jobs for all while reducing the savage and destructive inequalities that pervade our society. Compared with what the United States has now, a much larger universe of publicly oriented financial institutions can play a crucial role in addressing these problems. We highlight the institutions that progressive activists have been working to build in the United States.

In the next section, we define and then describe the rationale for public banking and finance (PB&F) and suggest how PB&F could

significantly contribute to the type of financial system we need to confront major challenges facing the US economy. In Section II, we give a brief history of public banking and finance initiatives in the United States, including a discussion of the historical limits and problems these institutions have faced. Next, we survey current initiatives in PB&F and report on a series of interviews we have held with public banking activists who are trying to bring these initiatives to fruition. Section IV concludes by emphasizing that, to overcome the tight constraints against broadscale and effective public banking and finance in the United States, we need the Federal Reserve and other large public financial institutions to underwrite PB&F to the same degree that they have underwritten private finance over the last decades. And we need activists and democratic monitors to ensure that public banking and finance institutions are created, thrive, and do their jobs.

I. THE FAILURES OF CAPITALIST FINANCE AND THE NEED FOR PUBLIC BANKING AND FINANCE

In communist China in the 1980s, any proposal to utilize markets to achieve a policy goal had to be justified by appealing to some failing in the planning system. Similarly, in our capitalist economy, and in the economics field dominated by capitalist ideology and power, any argument for government intervention or provision must be justified by identifying some “failure” of the market. This doctrinal game becomes absurd when the failures of the market system are as widespread and profound as they are in the United States. This required “market failure” justification for state intervention also makes little sense when one recognizes that contemporary monetary and financial institutions would simply not exist if not for state sanctions and support, at least not in any stable and sustainable form. Banking and finance would cease to exist without government subsidies and the legal apparatus

that enforces contracts and allows banks to create money. In that sense, the state is at the very foundation of these activities, and it would be reasonable to expect that, in a democracy, communities should have a say in how these institutions are constituted and what services they provide to the people in return.

These days, one does not have to look far to identify examples of the state underwriting the capitalist financial system. In recent years, state expenditures to prop up and stabilize the financial system in the United States and elsewhere have been enormous. Estimates are that the Federal Reserve and the government spent as much as \$30 trillion to prop up the US financial system during the GFC.⁴⁵ During the COVID-19 pandemic, so far, the Fed and the Treasury Department have committed to spend “whatever it takes” to keep the financial system afloat, with economists suggesting numbers as high as \$8 trillion as an eventual price tag. Of course, no one really knows what the ultimate cost will be.

Even these astronomically high prices are merely the tip of the iceberg. The United States, along with most other large economies, spends billions of dollars to underwrite and structure the private financial system: the whole apparatus of banking regulators, tax subsidies, central banks, and the court system that adjudicates and enforces contracts.

In this sense, the public mandate underwrites not only the stability of the financial system, but modern finance’s very existence.

What price does society charge for these vast services provided to private finance? It varies over time and place. In practice, the

4 Better Markets, “\$20 Trillion: The Cost of the Financial Crisis,” February 22, 2017, bettermarkets.com/newsroom/20-trillion-cost-financial-crisis-3.

5 James Felkerson, “\$29,000,000,000,000: A Detailed Look at the Fed’s Bail-out by Funding Facility and Recipient,” Levy Economics Institute of Bard College Working Paper, no. 698 (2011).

terms under which public support for finance is provided — and what society gets in return for that support — strongly depend on the power relations between capitalist financial elites and the rest of society, including workers, industrialists, and the state. Racial and ethnic power relations are also crucial in determining the distribution of these benefits, as are the very structures of capital accumulation and technological relations.

Mainstream economists' rationale for public provision of finance, which rests on identifying "market failures," provides a weak foundation for public extraction of reasonable returns from private finance in exchange for state support. This approach assumes the near optimality of private finance as given, on its own and without government involvement. Social provision of financial services is assumed to be second rate and unnecessary unless proven otherwise: it is largely seen as "frosting on the cake." So, how high a price can society extract for Marshmallow Fluff?

The "market failures" that economists consider legitimate include: "externalities" — for example, stemming technological spillovers that high-tech innovation can create for companies other than those that invent and produce them; "public goods," such as a civic and democratic culture created in the public education system that contributes to social stability; and goods with large "economies of scale" that prevent a competitive market from providing sufficiently. Economists also recognize "financial instability" and the "lender of last resort" as justifications for public intervention. But here, the only public provision usually considered reasonable is to provide for the bankers and hope that will trickle down to stabilize the rest of the economy.

In effect, such rationales for public provision of finance focus on "filling gaps" that, for one reason or another, private financial institutions do not satisfy. Externalities and public goods can justify the government subsidizing student loans; technological spillovers

can justify the Defense Department’s Defense Advanced Research Project Agency (DARPA) engaging in research and development (R&D) and then transferring the results at subsidized rates to private business; economies of scale can justify subsidizing the operation of transportation systems and other infrastructure.

Looking at the problem this way, one goes on a hunt for gaps: small businesses have trouble getting loans, so you create a small business loan facility; many poor people and racial minorities do not have access to bank accounts and other banking services, so you create a financial inclusion bank. But as you keep looking, the gaps multiply: green finance; affordable housing finance for minorities; patient capital for long-term investing; long-term infrastructure finance; affordable and flexible education finance; low-cost retirement savings vehicles; low-cost insurance. The gaps go on and on. The hole swallows the bagel.

As this very long list of “gaps” shows, the private financial system in the United States doesn’t even do a good job at the things it is supposed to excel at. Banks charge excessive fees for simple banking services. Asset management companies and financial advisers have major conflicts of interest. Banks engage in highly risky activities, expecting bailouts when they get into financial trouble. Private equity firms strip businesses and households of their assets by loading them up with debts, leaving them without the wherewithal to pay decent wages or compete with other companies.⁶ In fact, some research has shown that, in the United States, the normal operations of our financial system contribute a negative value to the economy.⁷ The authors estimate that these

6 Eileen Appelbaum and Rosemary L. Batt, *Private Equity at Work: When Wall Street Manages Main Street* (New York: Russell Sage Foundation, 2014).

7 Gerald Epstein and Juan Antonio Montecino, “Overcharged: The High Cost of High Finance,” *Roosevelt Institute*, July 12, 2016, rooseveltinstitute.org/overcharged-high-cost-high-finance/.

normal operations reduced US income by one year's GDP (about \$22 trillion) between 1995 and 2020. Similarly, another study by the authors found that the financial system reduced the UK's GDP by the equivalent of two years' value over roughly the same period.⁸

In this situation, as in many important areas of social and economic life under capitalism, it is difficult to separate the market from its failures.

In short, the public provision of financial services should not merely try to do what the financial system does not. It should also do better at many of the things private finance already purports to do. Rather than merely "minding the gap," a PB&F institution should help restructure the financial system to better serve public needs, especially the short-term and long-term needs of the poor, the working class, and the planet.

Public Banking and Finance: What Is It?

Before going any further, we would do well to define the central concept in the essay: public banking and finance (PB&F).⁹ There is a vast and growing literature on public banking, where one finds various definitions of it.¹⁰ Generally, these stipulate that public banks ought to have one or more of the following characteristics:

8 Andrew Baker, Gerald Epstein, and Juan Montecino, "The UK's Finance Curse? Costs and Processes," *Sheffield Political Economy Research Institute*, 2018.

9 This discussion has benefited greatly from an interview we had with Thomas Marois, Department of Development Studies, SOAS, the University of London who is one of the most interesting researchers of public banking. Marois also shared with us an excellent unpublished book which has informed some of the discussion in this section.

10 See, for example, Thomas Marois, "Towards a Green Public Bank in the Public Interest," UNRISD Working Paper, 2018; Gerald Epstein and Devika Dutt, "Public Banks, Public Orientation and the Great Financial Crisis of 2007-2008," in *Financial Innovation and Resilience* (Springer, 2018), 327-43; Robert C. Hockett and Saule T. Omarova, "Public Actors in Private Markets: Toward a Developmental Finance State," *Washington University Law Review* 93 (2015): 103.

1. public ownership
2. a public mandate
3. not driven mainly by profit maximization
4. a public/social/stakeholder orientation

Note that, according to this perspective, public ownership is not a necessary condition for a financial institution to be a public bank. Nor, as Thomas Marois emphasizes, is it a sufficient condition on its own.¹¹ Some financial institutions are owned by the government but support self-serving and even corrupt activities by governmental leaders. Similarly, a financial institution might have a social or stakeholder orientation and be privately owned.

In this essay, when we discuss PB&F, we generally mean financial institutions that have public support, have a social or public goal, and are not driven mainly by profit motives. Still, the precise structures and ownership characteristics of such institutions can vary. Marois's solution to this conundrum is that public banks are what public banks do: if a financial institution walks like a duck, and quacks like a duck, then it's a duck. By this perspective, a financial institution that serves as a public bank in one decade can be perverted or undermined and act quite differently in a subsequent decade, even though its "formal" ownership structure or charter has not changed at all. Thus, it is crucial to keep an eye on the actual activities of these institutions. Watch what they do, not what they say.

In this essay, we refer to these "ducks" as public banks and finance institutions (PBFIs). We have added the term "finance" to the more typical moniker, public banks, because in a market-based

11 Marois, "Green Public Bank."

financial system like the United States, non-bank finance is huge — and therefore, having strong, publicly oriented, non-bank finance becomes crucial.

There are many different kinds of PBFIs, but they typically fall into one of several categories. *Retail banks* are deposit-taking institutions with branch networks that provide regular banking services for individuals, households, small businesses, corporations, and governments. *Development banks* do not typically accept personal deposits or offer personal banking services, but instead specialize in accessing cheaper sources of capital, supporting long-term investments, employment, and providing technical expertise to commercial banks, other institutions, firms, and governments. Some of these are *bankers' banks*: they provide liquidity and clearing facilities, technical assistance, emergency lines of credit, and credit supplies and underwriting for smaller public banks. *Universal banks* combine both these functions, taking deposits and offering regular banking services while providing funds, services, and expertise for longer-term development.¹²

Ten Potential Benefits of PB&F in the United States

In light of this approach, here are ten important functions PB&F could play in our economy.

1. *Competition and regulation*: Public options function as competition for existing financial institutions, thereby providing people with alternatives to private finance and possibly improving the products and services that private finance offers. The public option also provides a means of regulating private financial institutions through competition.¹³

12 This paragraph draws on work from Thomas Marois. We thank him for sharing this work with us.

13 Mark Paul and Thomas Herndon, "A Public Banking Option as a Mode of Reg-

2. *Public goods*: Public goods, such as a highly educated population, efficient infrastructure, and long-term technological innovation with broad positive spillovers, can be supported by public finance institutions.
3. *Collective goods and complementarities*: Robert Hockett and Saul Omarova¹⁴ describe collective goods as those that require concerted and collective action to come to fruition and generate productive outcomes. Mehrsa Baradaran implicitly uses this concept in developing her proposal of “A Homestead Act for the 21st Century,” designed to provide housing for and revitalize poor neighborhoods.¹⁵ In Baradaran’s analysis, providing affordable housing is not sustainable in and of itself because there are a number of complementary goods that must be available at the same time, such as jobs, financial institutions, and grocery stores. Here, community development is a good that must involve collective planning and simultaneous financing in a number of different areas for any of the pieces to succeed. PB&F can be a useful mechanism to coordinate these activities.
4. *Crowding in*: Critics have argued that public provision of finance will crowd out private economic activity. But in many cases, it could have the opposite effect, bringing in more private investment. For example, the vast expenditure by the Defense Department on research and development has generated

ulation for Household Financial Services in the United States,” Roosevelt Institute, August 14, 2018, rooseveltinstitute.org/public-banking-option/. William Darity Jr, Darrick Hamilton, and Rakeen Mabud, “Increasing Public Power to Increase Competition: A Foundation for an Inclusive Economy,” Roosevelt Institute, May 2019.

14 Robert C. Hockett and Saule T. Omarova, “Private Wealth and Public Goods: A Case for a National Investment Authority,” *Journal of Corporation Law* 43 (2018): 437.

15 Mehrsa Baradaran, “A Homestead Act for the 21st Century,” *The Great Democracy Initiative*, May 2019, greatdemocracyinitiative.org/document/21st-century-homestead-act/.

highly lucrative corporate activity, such as from IBM, Apple, and Google.

5. *Financial inclusion — fighting poverty, exploitation, and racial discrimination*: Financial exclusion, exploitation, and racial injustice are deeply ingrained social ills in the United States. PBFIs can help finance affordable housing; cooperatives; small businesses; education initiatives; financial services: all in communities of color and for institutions owned or controlled by members of the community.¹⁶
6. *Financial resilience and stability*: PBFIs, by contributing to a diverse financial ecosystem, help to make the financial system more resilient and robust. For example, unlike for-profit banks, publicly oriented financial institutions tend to perform countercyclically, helping to stabilize the economy rather than exacerbating crises.¹⁷
7. *Economic transformation*: For large-scale transformative issues, the social provision of finance will play a major role. These include long-term gestation periods, massive uncertainty, large economies of scale, and the need for complementary investments and planning. One example is the pressing need to make the transition to renewable and non-carbon-producing fuels, such as the Green New Deal. This requires investment in new technologies and infrastructure implementation. In such a multifaceted transformative endeavor, public provision of finance is crucial as a facilitating mechanism and a planning tool.

16 Mehrsa Baradaran, *The Color of Money: Black Banks and the Racial Wealth Gap* (Cambridge: Harvard University Press, 2017).

17 Epstein and Dutt, "Public Banks, Public Orientation."

8. *Promote full employment and good jobs*: Credit allocation is key for job creation, including areas of structural unemployment, as well as patient capital for long-term gestation projects and infrastructure investments. Here, the quality of employment is as critical as the quantity (“high road” employment).
9. *Instrument of public policy*: In an economic transformation like the Green New Deal, public provision of credit is a powerful instrument of government policy. Countries that have made successful, rapid, and transformative economic changes, including the United States, South Korea, Taiwan, China, and Europe after World War II, all used public provision of finance as a carrot or stick to elicit desired corporate behavior and allocate credit to priority sectors.¹⁸
10. *Reducing the power of financial elites and countering capital strike*: Among the most important effects of PB&F — and a key reason capitalists often oppose it — is that having a public option reduces the market power of private capital and the political power of finance. Banks and other financial activities in the United States have become more concentrated, so that social provision will confront these oligopolies with more competition. Politically, public options reduce the power of the threat of a capital strike and of being “too big to fail.” With a

18 Alice Amsden, *The Rise of “the Rest”: Challenges to the West from Late-Industrializing Economies* (New York: Oxford University Press, 2001); Gerald Epstein, “The David Gordon Memorial Lecture: Finance without Financiers: Prospects for Radical Change in Financial Governance,” *Review of Radical Political Economics* 42, no. 3 (September 2010): 293–306, <https://doi.org/10.1177/0486613410375416>; John Zysman *Governments, Markets, and Growth: Financial Systems and the Politics of Industrial Change* (Ithaca: Cornell University Press, 1983); Barry Eichengreen, *The European Economy Since 1945: Coordinated Capitalism and Beyond* (Princeton: Princeton University Press, 2008), <https://doi.org/10.2307/j.ct-t7rpf5>; Robert Pollin, “Financial Structures and Egalitarian Economic Policy,” *New Left Review*, November/December 1995.

large PB&F footprint, we can say to Wall Street, “Go ahead and fail. Our PBFIs will provide the needed services without you.” This possibility is not sufficiently emphasized in discussions of public banking. Moreover, PBFIs provide a counterweight if private finance threatens capital flight in response to progressive policies they don’t like.¹⁹

Essential Finance in the United States to Confront Four Clear and Present Dangers

We have described ten functions that public banking and finance (PB&F) ought to serve in contemporary capitalism, focusing especially on the United States. But for our current historical conjuncture, we want to focus on the problems facing us that are especially important now.

At the moment, we are confronting four pressing economic and social challenges: recovery from the COVID-19 pandemic; demands for racial, social, and economic justice; the need to transition to a carbon-free economy; and addressing worsening economic and political inequality and unemployment.

Here are six specific ways that public banking and financial institutions can address these issues.

1. Provide a simple, efficient, and universally available payment mechanism. The lack of one has been demonstrated clearly by the great difficulties the US government has had in making funds quickly available to individuals and businesses during the COVID-19 crisis.
2. Offer universal access to short-term, emergency borrowing at fair costs and interest rates. With few having sufficient liquid

19 James Crotty and Gerald Epstein, “In Defense of Capital Controls” *Socialist Register*, 1996. And James Crotty, *Keynes Against Capitalism; His Economic Case for Liberal Socialism*. New York: Routledge, 2019.

assets available in the face of an economic emergency, and with credit access usurious at best, the COVID-19 crisis has revealed the high social cost of our banking system's low accessibility.

3. Channel significant financial resources to businesses, non-profits, and cooperative institutions so they can survive emergencies and thrive in normal times. Many small businesses, cooperative institutions, and nonprofits have limited access to financial institutions for credit, and when they do, this access usually comes at a steep price.
4. Finance the transformation to a clean energy economy. Effective financial institutions will be required to mobilize and channel these funds in a timely and inexpensive way.
5. Finance infrastructure for a high-productivity economy, create full employment, and raise wages. Financial institutions that allocate "patient" capital for pressing social investments are required.
6. Address poverty and discrimination, and contribute to decent wages. Fixing major social problems, including racial discrimination in housing, jobs, business creation, and education; affordable housing shortages; and infrastructure provision, will require significant resources and financial institutions. Long-term socially and racially diverse capital accumulation must be appropriately funded. Many of the funds for capital investment in the United States are not only short-term oriented and discriminate based on race and gender, they also discriminate against unorthodox "business models" such as cooperative enterprises. Patient capital needs to be made available to foster widely shared prosperity and non-capitalist institutional models.

If these problems are to be effectively addressed, PB&F must play a major role in financing their solutions. But we must acknowledge that these problems are diverse, and so is the United States — geographically, demographically, and culturally — with a deeply rooted market-oriented system. The development of PB&F has to take into account these initial conditions. To carry out these functions, we will need a combination of public and private/cooperative financial institutions (some large and centralized, many smaller and decentralized), a range of ownership and organizational structures, and strong public-oriented government institutions, such as the Federal Reserve, to create an environment in which these different kinds of financial institutions can thrive.

Can Public Banking and Finance Institutions Thrive and Survive in a Capitalist Economy?

Capitalist economies, especially those dominated by neoliberalism, would seem to be a uniquely inhospitable place for public banking and finance. Yet, as Thomas Marois has documented, there has been a dramatic increase in PB&F's prevalence around the world in recent decades.²⁰ According to him, almost 700 public banks currently exist. Altogether, they control 20 percent of all bank assets, public and private. While it is true that public control of banking assets has probably fallen from its 1970s height of around 40 percent, today's economies are much bigger, and the total mass of public bank capital has grown substantially. A conservative estimate by Marois shows that public banks have combined financial assets totaling \$38 trillion, which equals 48 percent of global GDP.

How can PB&F continue to thrive in the apparently hypercapitalist environment of most countries? Two factors are pivotal.

20 Marois, "Green Public Bank."

The first is one we have discussed earlier: the recent decades of financial crises, and especially the GFC, have led to the growth of PBFIs to rescue finance, if not the economy as a whole. The second may be a bit more surprising: in some ways, PBFIs are actually more efficient and safer than private financial institutions.

Some Competitive Advantages of PB&F

Despite the dominant economics claim to the contrary, there are some competitive advantages of PB&F that allow them a fighting chance, even in the capitalist marketplace, despite the fact that their mission is to address the social goals and services that private banks avoid.

These advantages include:²¹

1. PBFIs tend to emphasize “*relationship*” banking so that bankers and customers get to know each other well; this increases knowledge of credit risks and enhances trust, thereby reducing manipulative or fraudulent behavior on both sides.
2. *Public mandates and lack of shareholder control* typically lead PBFIs to adopt less risky behavior than their private counterparts. This can result in less instability.
3. *Access to capital at lower cost*: Many PBFIs have lower costs for capital because they are perceived as being safer than private banks that engage in high-risk activities. PBFIs tend to build capital through profit retention, since they are not under pressure to distribute dividends to shareholders, and they do not face the same shareholder demands for rapid expansion.

21 This paragraph draws on: Olivier Butzbach and Kurt von Mettenheim, “Explaining the Competitive Advantage of Alternative Banks: Toward an Alternative Banking Theory?”, in Olivier Butzbach and Kurt von Mettenheim, eds., *Alternative Banking and Financial Crisis* (Pickering & Chatto, 2014), Chapter 4.

4. *Public mandates lead to banks passing on advantages to customers:* PBFIs pass on lower expenses to customers rather than needing to pay extraordinarily high executive salaries and large amounts of dividends. This attracts more borrowers and more depositors and lenders.
5. *Economies of scale:* Even though relationship banking and tight monitoring of credit risks can be very costly, PBFIs can achieve economies of scale by joining PB&F networks that provide services like underwriting, technical assistance, and help identifying lenders and good borrowers. Such networks can at least partially erode some of the advantageous economies of scale that large private firms have.

Despite these possible advantages in efficiency, PB&F is nonetheless relatively small and disadvantaged in the United States compared with many other countries. Why is the United States a relative outlier in this regard? A look at the history of public banking in the United States can offer some clues.

II. A HISTORY OF PUBLIC BANKING AND FINANCE IN THE UNITED STATES

There have been numerous examples of state-supported public-oriented finance throughout US history. These were mandated under a variety of circumstances: some to meet a national emergency or war, others to achieve government development goals, and still others to do the bidding of regional, sectoral, or capitalists' interests. Some were developed in response to working-class or agrarian organizing and their demands for access to credit and financial services, and others in response to the organization and demands of racial minorities. Each of these initiatives has its own founding stories, but as a first pass, one could say that the more

progressive ones were won through grassroots struggle and the mobilization of political power.

Many of these initiatives were effective in achieving their goals, at least for a period of time. But apart from those that were designed to bail out banks and other financial institutions, many state-organized financial institutions eventually faltered, usually as a result of fierce political opposition and sometimes due to corruption and co-optation by private financiers.²² The majority of those that did survive were kept small and relatively ineffective in achieving the goals envisioned by those who fought for their creation.

This common constriction of PB&F is a result of the general dominance of our economic and political institutions by capitalist ideology and the power of finance. In countries with an influential socialist or social-democratic political culture, socially oriented financial institutions are much more likely to survive and even thrive than in the inherited structures of the United States. As Thomas Marois notes, the creation and evolution of PB&F institutions are shaped by the relative powers of different classes and ideologies in a hypercontested space of capitalism: finance. That is why the political power advocates can amass through activism is crucial to PB&F's future in the United States.

State support for financial institutions is inherent to the very nature of finance. The question is whether these financial institutions serve public purposes, and how well they do so. Historically, there have been many state-supported financial institutions that effectively promoted social and public purposes, at least for a time.

22 For a useful short history, see: Mehrsa Baradaran, *How the Other Half Banks: Exclusion, Exploitation, and the Threat to Democracy* (Cambridge: Harvard University Press, 2015). On the populist movement of the late nineteenth century, see Lawrence Goodwyn, *Democratic Promise: The Populist Moment in America* (New York: Oxford University Press, 1976).

Apart from those associated with national emergencies or bailing out the banking system itself, successful initiatives have usually resulted from political organization, agitation, and the amassing of political power. Nonetheless, many of these successes were difficult to sustain. Preserving the mission of such institutions in the face of political and economic pressure from private finance, as well as responding effectively to financial innovation and structural changes, proved to be extremely challenging. Truly effective PB&F requires continuous support from the government and the vigilance of progressive political forces.

The State-Finance Nexus

The links between publicly oriented finance and the state go back hundreds of years.²³ Some of the earliest relations were between the church, philanthropic organizations, and banks, as, for example, in fifteenth-century Naples.²⁴

During the eras of state building and dynastic wars in Europe, the linkages between sovereign states and banks increased dramatically. The direction of financial support initially went from banks to the state, with European banks financing wars, conquest, and lavish royal consumption. Eventually, the broad direction of support changed, with states giving financial institutions charters and monopolies over note issue, and then ultimately became bidirectional, with banks and states creating public-private partnerships to fund regional and national infrastructure, commerce, and other social goals.

In the United States, public banks were created early in the development of the nation. The first was the Bank of Pennsylvania,

23 See Baradaran, *How the Other Half Banks*, Chapter 2.

24 Lilia Costabile and Larry Neal, eds., *Financial Innovation and Resilience: A Comparative Perspective on the Public Banks of Naples (1462-1808)* (London: Palgrave Macmillan, 2018).

a public bank established to help feed troops during the American War of Independence.²⁵ Alexander Hamilton saw these early banks as a way to finance the development of the new country, but he met great political opposition. With victory in the war, publicly founded banks began to multiply. This connection between state and finance was well described by Bray Hammond, the scholar of early American finance: “The community, whether shrewdly or not, had adapted private initiative and wealth to public purposes, granting privileges and exacting duties in return . . . there persisted a strong conviction that a [bank’s] charter was a covenant.”²⁶ This inherently public nature of banking was a recurrent theme throughout US history. In 1911, for example, the Kansas Supreme Court explained that banking is not a “matter of private concern only, like the business of the merchant, and for all purposes of legislative regulation and control it may be said to be ‘affected with a public interest.’”²⁷

Historically, there was great ambivalence in the United States over the desirability of big finance, especially big national banks, with conflicts between Hamilton and Thomas Jefferson over the first bank of the United States, and Andrew Jackson’s opposition to the second bank. Yet despite these clashes, the United States would return, time and time again, to public-oriented financing during both national emergencies and periods of extraordinary economic transformation.

The federal government issued “greenbacks” to help finance the Civil War, a massive government financial intervention.²⁸ The

25 Baradaran, *How the Other Half Banks*, 27.

26 Bray Hammond, *Banks and Politics in America: From the Revolution to the Civil War* (Princeton: Princeton University Press, 1957), as quoted in Baradaran, *How the Other Half Banks*, 28.

27 Baradaran, *How the Other Half Banks*, 33

28 Christine A. Desan, “The Monetary Structure of Economic Activity,” Harvard

establishment of the national banking system in the 1860s and the creation of the Federal Reserve System in 1914 were more interventions in the financial system by the US government.²⁹ In 1911, the federal government established the Postal Savings System, which survived until 1967. The postal system banks provided easy access to savings accounts and payment services through US post offices. Much of the early public financial innovations aimed to help agriculture. For example, in 1916, soon after the creation of the Federal Reserve, the government created twelve federal land banks that encouraged the formation of hundreds of national farm loan associations. In the wake of the Great Depression of the 1930s, Herbert Hoover and then Franklin Roosevelt and their governments created a myriad of financial institutions to rescue the economy and finance farming, housing, critical production, and underwriting the war effort. These institutions included the Reconstruction Finance Corporation (RFC) to support industry, real estate, and housing; the Farm Credit System; the Federal Home Loan Bank System; and several government-sponsored enterprises, including Fannie Mae and Freddie Mac, directed at supporting the housing market.³⁰

Important public financing initiatives also took place at the state and local levels. Perhaps the best known is the Bank of North Dakota (BND). Established in 1919, the BND serves as a model and inspiration for many current public banking activists.

The origins and operations of the BND provide an example of successful resistance to the purely market-oriented logic of the

Public Law Working Paper no. 20-04, 2020, <https://doi.org/10.2139/ssrn.3557233>.

29 Desan, "The Monetary Structure."

30 Kurt von Mettenheim and Olivier Butzbach, "The United States: Alternative Banking from Mainstream to the Margins," in *Alternative Banking and Financial Crisis*, 185-94.

banking industry in the United States.³¹ The BND was born out of a campaign by the populist Nonpartisan League, which was a political party formed by farmers, reformers, and radicals fighting against the monopoly power of the business institutions dominating North Dakota in the early twentieth century. The League initially aimed at establishing a system of rural credit unions, farm cooperatives, state-run mills, packing houses, and cold-storage plants that would serve the needs of the people.³² In 1919, the North Dakota legislative session, taking its cues from the league's industrial program, created the BND. The legislation declared the bank's purpose as "providing low-cost rural credits, financing state departments and enterprises, and serving as a clearinghouse and rediscount agency for banks throughout the state."³³

Today, the BND implements the so-called state partner bank model. In this model, the state of North Dakota deposits public funds in the BND. The BND then partners with local lenders, including local banks, credit unions, and other financial service providers, to provide the residents of North Dakota with high-quality and low-cost access to financing. Local lenders originate loans for agricultural producers, small businesses, and residential mortgages. The BND, in turn, partners with these banks by purchasing the loans from the originators. The BND, in a way, acts as a "banker's bank." Partnering with the BND enables the banks to

31 Marc Schneiberg, "Lost in Transposition? (A Cautionary Tale): The Bank of North Dakota and Prospects for Reform in American Banking," in Michael Lounsbury and Eva Boxenbaum, eds., *Institutional Logics in Action, Part A*, Research in the Sociology of Organizations 39 Part A (Bingley: Emerald Group Publishing Limited, 2013): 277-310.

32 Chad Hatzenbuehler, "The Birth of the Nonpartisan League," The BND Story, accessed May 30, 2020, thebndstory.nd.gov/the-early-years/the-nonpartisan-league/.

33 Hatzenbuehler, "Nonpartisan League."

originate loans that exceed their legal or internal lending limits.³⁴ Hence, the existence of the BND enhances the viability of small banks in North Dakota and strengthens them in competing against large out-of-state banks.

The operations of the BND amount to an alternative, decentralized, and regionally based circuit of capital that is used to the benefit of small businesses, farmers, local governments, and students. The bank channels the funds collected from state institutions to support economic development.³⁵ The BND does not use these funds in national or global financial markets to invest in derivatives or any other risky and speculative economic activity.

The resilience of the BND in the wake of the GFC has piqued widespread interest in the bank. Various studies found that, during the crisis, the BND remained profitable and had a better credit rating than most privately owned banks, while increasing its loans and letters of credit to North Dakota banks that required liquidity. This greater resilience is consistent with the literature on public-oriented banks in other parts of the world.³⁶

The COVID-19 crisis has further demonstrated the effectiveness of the BND. While many small businesses in other states struggled to access the Paycheck Protection Program (PPP), small businesses in North Dakota managed to secure more PPP funds relative to the state's workforce.³⁷ As the BND and North Dakota banks were working efficiently to allocate PPP funds, a series of

34 Yolanda K. Kodrzycki and Tal Elmatad, "The Bank of North Dakota: A Model for Massachusetts and Other States?" FRB of Boston Public Policy Discussion Paper, no. 11-2, papers.ssrn.com/abstract=1932426.

35 Schneiberg, "Lost in Transposition."

36 Epstein and Dutt, "Public Banks, Public Orientation."

37 Andrew Van Dam, "North Dakota Businesses Dominated the PPP. Their Secret Weapon? A Century-Old Bank Founded by Radical Progressives," *Washington Post*, May 15, 2020, [washingtonpost.com/business/2020/05/15/north-dakota-small-business-ppp-coronavirus/](https://www.washingtonpost.com/business/2020/05/15/north-dakota-small-business-ppp-coronavirus/).

class action lawsuits were being filed against Bank of America, Wells Fargo, and JPMorgan Chase for attempting to maximize the fees they earned from distributing loans.³⁸

Critics often argue that BND's resilience during the GFC stemmed from the loans it made to profitable state industries, including oil. By emphasizing its particularities, critics often project the BND as an irrelevant experience inapplicable to other contexts. The BND's investment in oil clearly contradicts the current demands of public banking advocacy groups (see below). Nevertheless, the BND provides a proof of concept for how a public bank could operate in the United States. It illustrates the enormous capacity of public banks to respond to local interests. Through a publicly agreed-upon charter, there is no reason why public banks in other states cannot direct their investment toward green energy and green jobs.³⁹

During the Great Depression, the US government, in addition to establishing agricultural, housing, and industrial financing institutions,⁴⁰ implemented legislation to facilitate the creation of not-for-profit financial institutions to service households. Specifically, in 1934, Congress passed the Federal Credit Union Act, which embraced credit unions as critical institutions that can address the credit needs of the working classes.⁴¹

Credit unions were born to empower farmers and workers whose credit needs were not adequately served by existing

38 Jake Tonkel and Nick Cortez, "Op-Ed: Public Banking Can Recharge South Bay's Economy," *San Jose Inside*, May 12, 2020, sanjoseinside.com/opinion/op-ed-public-banking-can-recharge-south-bays-economy/.

39 Eillie Anzilotti, "The One Strategy That Could Finance the Whole Green New Deal," *Fast Company*, June 26, 2019. fastcompany.com/90364616/public-banking-can-finance-the-green-new-deal.

40 Such as the Reconstruction Finance Corporation (RFC).

41 Mettenheim and Butzbach, "The United States: Alternative Banking"; Baradaran, *How the Other Half Banks*.

banking facilities.⁴² They are structured as member-owned non-profit cooperatives providing services to a designated group, such as government employees, association members, or residents of a geographic area. This common bond requirement was introduced to use personal knowledge about the members to offset the risk of lending to low-income earners. This feature tailored credit unions to serve the needs of low-income earners. Furthermore, their tax-free status helped credit unions to compete with commercial banks in these markets. The Federal Credit Union Act introduced a “one member, one vote” principle that gives each member voting rights independent of the amount of money they hold in their accounts.

The aggregate performance of credit unions, in terms of net income, late loans, net charge-offs, asset growth, and loan growth, compare favorably with commercial banks. Despite their better performance, credit unions still retain a much smaller market share than private banks and many other financial institutions.

Initially, the functions of credit unions were limited to providing inexpensive loans to their low-income members. Due to regulatory burdens, credit unions started losing customers and sought deregulation that would allow them to offer more attractive interest rates. Congress responded to these requests positively, leading to a change of mission whereby they lost their focus on poverty alleviation. Over time, credit unions switched from institutions supporting low-income earners into ones that would compete with commercial banks to serve the middle class.

Despite these regressive changes, credit unions still constitute an alternative to the purely profit-oriented logic of privately owned commercial banking. In general, they are less subject to

42 Mehrsa Baradaran, “How the Poor Got Cut Out of Banking,” *Emory Law Journal* 62, no. 3 (2012): 483.

pressures to maximize shareholder value compared to the commercial banks.⁴³ Even though they, too, invest in mortgage-backed securities, collateralized debt obligations, and other types of derivatives, they do so less aggressively than commercial banks.⁴⁴ They are more oriented toward serving their members than charging them an endless stream of fees. They return their profits in the form of lower interest rates on lending and expanded services. There are also some credit unions, called community development credit unions (CDCUs), that are specifically designed to serve low-income groups. CDCUs have the potential to direct more resources to underserved communities.

Community development financial institutions (CDFIs) represent an important component of public-oriented finance, some elements of which are still present. CDFIs are mission-driven organizations that aim to provide services that create and broaden economic opportunities within their communities.⁴⁵ They comprise a range of institutions whose primary goal is to improve the economic conditions of low-income individuals and communities.⁴⁶ For-profit community development banks, nonprofit CDCUs, and community development venture capital funds are all examples of CDFIs. These entities provide financial services that are often not available from mainstream institutions.⁴⁷

43 Marc Schneiberg, "Toward an Organizationally Diverse American Capitalism? Cooperative, Mutual, and Local, State-Owned Enterprise," *Seattle University Law Review* 34 (2010): 1409.

44 Schneiberg, "Toward an Organizationally Diverse."

45 Stephanie Geller, "Community Development Financial Institutions," *TheNextSystem.org*, March 16, 2020, thenextsystem.org/learn/stories/community-development-financial-institutions.

46 Lehn Benjamin, Julia Sass Rubin, and Sean Zielenbach, "Community Development Financial Institutions: Current Issues and Future Prospects," *Journal of Urban Affairs* 26, no. 2 (June 2004): 177-95. doi.org/10.1111/j.0735-2166.2004.00196.x.

47 Schneiberg, "Toward an Organizationally Diverse."

The roots of CDFIs can be traced back to the efforts of community activists who were fighting redlining in urban areas and seeking to redirect capital toward community-controlled banks.⁴⁸ The first banks targeting low-income neighborhoods were established in the late 1880s.⁴⁹ The 1930s and 1940s witnessed the emergence of credit unions designed to serve low-income earners and African Americans who lacked access to credit. During the 1980s, nonprofit loan funds began working toward promoting affordable housing and small business development.⁵⁰

There was an attempt to provide a more organized form to these various initiatives in the 1990s through the establishment of the CDFI Fund and renewed implementation of the Community Reinvestment Act.⁵¹ The fund aimed to increase the availability of affordable capital in areas that were historically underserved and discriminated against. To date, it focuses on fostering the development of loan funds, credit unions, and other financial institutions whose primary mission is to serve low-income communities. It also certifies organizations as CDFI to ensure that they meet certain criteria.⁵² Currently, there are more than 1,100 CDFIs operating throughout the country. CDFIs have the potential to transform

48 Geller, "Community Development Financial Institutions."

49 W. E. B. Du Bois, "Economic Co-Operation among Negro Americans," Atlanta University Press, 1907. Cited in Benjamin et al., "Community Development Financial Institutions."

50 Benjamin et al., "Community Development Financial Institutions."

51 The Community Reinvestment Act (CRA), enacted in 1977, mandated banks to address the needs of their entire service area and prohibited them from discriminating against any portion of their markets (Benjamin et al., "Community Development Financial Institutions"). However, for at least fifteen years, the CRA was largely unenforced. The revision of the CRA in the 1990s required banks to be judged on their actual lending practices in low-income communities. While these changes contributed to increased lending, the problem of redlining and underinvestment in low-income communities persists.

52 Benjamin et al., "Community Development Financial Institutions."

neighborhoods that suffered from historical disinvestment by providing capital that can be used to develop new businesses, affordable housing, and community spaces.⁵³ But, for the most part, they remain small, and their contributions are not adequate to address the problems of poverty and lack of investment in our cities and housing in the United States.

III. PB&F: A RESURGENCE OF ACTIVISM

The inefficiencies and excesses of the existing financial system revealed once again by the GFC have triggered a growing interest in alternative banking arrangements in the United States. The infrastructure problems in US cities, the exclusion of millions of Americans and especially people of color from essential banking services, and the private banking system's pernicious record of funding environmentally harmful projects have further fueled interest in a public and socially oriented banking and finance movement across the country.⁵⁴

To better understand this movement and the activists driving it, we held a series of (remote) interviews with a number of them over several months in the spring and early summer of 2020⁵⁵. Our discussion in this section is informed by these interviews as well as websites, reports, and secondary literature.

53 Geller, "Community Development Financial Institutions"

54 Sarah Jones, "Why Public Banks Are Suddenly Popular," *New Republic*, August 10, 2018, [newrepublic.com/article/150594/public-banks-suddenly-popular](https://www.newrepublic.com/article/150594/public-banks-suddenly-popular).

55 We gained valuable insights from the following list of organizers, activists, and scholars through interviews and email exchanges: Michael Brennan (Public Banking Institute), Rick Girling (San Francisco Public Bank Coalition and California Public Banking Alliance), Ben Gordon (California Public Banking Alliance), Austin Sachs (Protect US), Thomas Marois (SOAS), Steve Seuser (DC Public Banking), Barbara Clancy (Mass Public Banking), Earl Staelin (Rocky Mountain Public Banking) and the participants of the National Public Banking Alliance Monthly Zoom Meeting, June.

The Agenda of Public Banking Advocacy in the United States

The resurgence in activist interest in public-oriented finance represents the pressing economic, social, and environmental needs of our communities.

Environmental justice is one of the core principles of almost all public banking advocacy groups in the United States. Public banking advocates rightly point out the worldwide failure of private banks to pull their weight in climate finance despite having far higher numbers and more assets than public banks⁵⁶. For instance, of the \$454 billion invested in climate finance in 2016, public and private banks invested almost equal amounts in green investment, despite the fact that the former controls only 20 percent of total banking assets.⁵⁷ In the context of the failure of private banking to meet the needs of the environmental transition, there is a growing belief that public banking should finance green transitional infrastructure in the United States. The Green New Deal resolution drafted by Representative Alexandria Ocasio-Cortez and Senator Ed Markey cites public banking as an option in its financing. The Next System Project's proposal for a green investment bank, put forward by Thomas Marois and Ali Rıza Güngen, explores public banking in the context of financing the Green New Deal.

The lack of access to basic and low-cost financial services by a large portion of the US population is another major issue the public banking movement aims to address. According to some estimates, individuals without bank accounts, often referred to as "unbanked" or "underbanked," end up spending an average of 10

56 Thomas Marois and Ali Rıza Güngen, "A US Green Investment Bank for All: Democratized Finance for a Just Transition," The Next System, September 20, 2019, accessed May 30, 2020, thenextsystem.org/green-investment-bank.

57 Marois and Güngen, "A US Green Investment Bank."

percent of their annual income on fees to cash checks, purchase prepaid debit cards, or use third-party services such as Western Union to send and receive money.⁵⁸

The maintenance of checking and savings accounts costs banks money — around \$250 every year.⁵⁹ Banks hire staff, pay for buildings, invest in technology, and build ATMs to maintain basic banking services. Given their profit-maximizing goals, banks reject the customers who are deemed unprofitable or repel them with punishing fees. According to the Federal Deposit Insurance Corporation, overdraft fees, service charges, and minimum balance requirements are among the main reasons people do not open bank accounts.⁶⁰

The COVID-19 pandemic has further highlighted problems with access to financial services. As a part of the CARES Act, Congress agreed to distribute checks worth \$1,200. A few weeks after the decision, millions of Americans received their stimulus checks, while unbanked or underbanked Americans expect to wait longer for their checks and pay fees up to 10 percent to cash them.⁶¹ To facilitate the distribution of COVID-19 stimulus checks, several lawmakers, including House Speaker Nancy Pelosi and Representative Rashida Tlaib, proposed that the Fed offer digital accounts to Americans through the United States Postal Service (USPS) — but these proposals were not included in the legislation.⁶²

58 Mehra Baradaran, “Rethinking Financial Inclusion: Designing an Equitable Financial System with Public Policy,” Roosevelt Institute, April 16, 2020, rooseveltinstitute.org/rethinking-financial-inclusion-equitable-financial-system-public-policy/.

59 Baradaran, “Rethinking Financial Inclusion.”

60 Cited in Baradaran, “Rethinking Financial Inclusion.”

61 Baradaran, “Rethinking Financial Inclusion.”

62 Jeff Spross, “We Need to Send People Money. We Need to Fix How They Get It, Too,” *The Week*, March 28, 2020, theweek.com/articles/905207/need-send-people-money-need-fix-how.

Postal banking has indeed been one of the focal points of public banking advocacy in the United States. A postal banking system was in place in the United States between 1911 and 1966 that provided basic banking services to low-income, rural, and immigrant households.⁶³ Public banking options similar to postal banks are still in use in more than sixty countries, and they are shown to mitigate financial exclusion. Postal banking advocates argue that USPS can address financial exclusion by providing basic banking services such as deposits, bill paying, check cashing, and small loans. One advantage of reestablishing postal banking is that USPS already has an office in each ZIP code. Indeed, 59 percent of USPS offices are located in ZIP codes with either single or no bank branches exempting postal banking from major infrastructure problems.⁶⁴

The socially productive use of state resources is another agenda item of public banking advocacy groups. Private banks charge local governments hefty fees to keep their deposits and provide cash management services. According to Public Bank LA, the city of Los Angeles pays about \$100 million a year in banking fees and interest. Furthermore, most private banks use these funds to engage in practices that are inconsistent with many communities' values, such as predatory lending practices, funding private prisons and detention centers, and investing in environmentally harmful activities. Advocates believe that by reducing fees and interest payments, public banks can help states save money and channel these funds into socially productive investments, such as community housing. For instance, advocates in California claim that public banking can serve to address astronomical housing prices and homelessness by supporting community housing.⁶⁵

63 Paul and Herndon, "A Public Banking Option."

64 Paul and Herndon, "A Public Banking Option."

65 Adam Simpson, David Jette, and Juleon Robinson, "The Campaign for Public

Many advocacy groups believe that public banking can address racial and gender inequalities. Private banking in the United States has a long history of redlining, whereby people in communities of color are denied loans, including mortgages. Notwithstanding the federal Community Reinvestment Act of 1977, the practice persists throughout the country.⁶⁶ Advocates suggest that public banking can address these issues by supporting businesses owned by people of color and initiating more equitable mortgage allocation. For instance, the 2018 proposal for a Public Bank East Bay in Oakland, California,⁶⁷ recommends that when making loans, the bank should support housing development, business owners from marginalized communities, and businesses that pledge to hire members of marginalized communities, including those who were formerly incarcerated, the homeless, and people with disabilities.

Public Banking Networks

In recent years, public banking activists have established a nationwide network of organizations, advocacy groups, and nonprofit organizations. The Public Banking Institute (PBI),⁶⁸ Demos,⁶⁹ and National Public Banking Alliance (NPBA)⁷⁰ are among the central nodes in the public banking advocacy network. PBI is a think

Banks, From Coast to Coast,” The Next System, November 2, 2018, accessed May 30, 2020, thenextsystem.org/learn/stories/campaign-public-banks-coast-coast.

66 Yuh-Line Niou and Maureen Genna. “City Limits: NY Can Reduce Redlining’s Residue by Backing Credit Unions,” New Economy Project, March 28, 2019, neweconomynyc.org/2019/03/city-limits-ny-can-reduce-redlinings-residue-by-backing-credit-unions/.

67 https://californiapublicbankingalliance.org/wp-content/uploads/2018/04/FOPB_public_bank_of_oakland_governance_proposal_040918.pdf

68 <https://www.publicbankinginstitute.org/>

69 <https://www.demos.org/>

70 <https://publicbanking.us/>

tank and education organization formed in 2011 to promote state and local publicly owned banking. Demos is a public policy and research organization based in New York and affiliated with the magazine *American Prospect*. NPBA is a recent initiative that aims to mobilize communities to advance socially and environmentally responsible public banks throughout the United States. These organizations have forged connections with an extensive collection of state-level policy groups and nonpartisan advocacy organizations to tap into existing coalitions and mobilize them to support legislation.⁷¹ They provide policy briefs and model laws to state officials and legislatures. They work directly with treasurers and legislators to introduce bills in their states, testify at hearings, and track bills' progress. As Marc Schneiberg puts it, these organizations operate as a clearinghouse for information about public banking legislation across the country.

North Dakota, home to the only state-level public bank in the United States, is a frequent reference point in almost any discussion on public banking, and not only because the Bank of North Dakota represents a thriving and resilient alternative to market-oriented banking (see above). It's also because the grassroots movements advocating for disinvestment campaigns against the Dakota Access Pipeline Project (DAPL) in North Dakota laid the groundwork for the most significant victory of the public banking movement in recent years.

In 2016, the DAPL, which projected a significant expansion of fossil fuel infrastructure, sparked massive protests for the water supply and livelihoods of the indigenous people of Standing Rock. #NoDAPL called on a global grassroots movement to advocate for disinvestment and prevent pipeline construction, and thousands of activities around the country participated. The activists ran

71 Schneiberg, "Lost in Transposition."

a divestment campaign against Wells Fargo, one of the fifteen banks lending to the DAPL project. The campaign focused on pulling some cities' deposits, including Seattle, San Francisco, Los Angeles, and Albuquerque, out of Wells Fargo accounts.⁷² Thanks to the efforts of #NoDAPL activists, in February 2017, the city councils of Seattle, Washington, and Davis, California, voted to end their relationship with Wells Fargo. But this raised an important question: Where should local governments put their money instead? The failure to meaningfully divest from Wall Street banks gave rise to the Public Bank LA initiative, which began advocating for the creation of a public bank owned by the city of Los Angeles, managing city funds in the public interest.

Public Bank LA managed to build support around a city referendum to facilitate its creation. Even though the referendum fell short of the support it needed at 44.15 percent, this momentum translated into the California Public Banking Alliance (CPBA), which represents a coalition of grassroots groups in ten cities across the state.⁷³ In October 2019, thanks to the efforts of CPBA, public banking advocates won a significant victory in California, as the state passed the first municipal banking legislation in the country, AB 857. This legislation authorized California to charter ten municipal public banks over seven years.

Advocates in California have also been campaigning for the establishment of a state-level public bank. In 2019, Democratic senator Ben Hueso introduced a bill, SB 528, which aimed to transform California's Infrastructure and Economic Development Bank (the IBank) into an institution that could take deposits from cities and countries and provide loan guarantees and conduit

72 Anzilotti, "One Strategy."

73 Michael Brennan, "Democracy in Banking: Modeling a State Partner Bank." Democracy Policy Network, forthcoming.

bonds to state projects that need financing. Although the bill failed, there is a new task force working toward converting the IBank into a state public bank. By July 8, 2020, a new bill, AB 310, was introduced to create a California state public bank. If it passes, this legislation will expand the lending capacity of the IBank and convert it into a depository bank that can leverage its capital up to ten times and direct its lending toward an equitable post-COVID recovery. With the prospect of establishing ten municipal banks and transferring the IBank into a state-level public bank, California has the potential to demonstrate public-oriented banking for the rest of the country.

Since 2009, more than thirty states have proposed legislation in support of public-oriented banking. According to PBI, there are organized community groups and candidates with public bank platforms in eleven states, in addition to the thirteen states that introduced feasibility studies between 2017 and 2020.⁷⁴ These initiatives are geographically widespread, including highly urbanized places like New York, California, and Massachusetts, as well as less populated states such as Maine, Montana, and Vermont.

Attempts to legislate public banking often start with feasibility studies that aim to find gaps in the existing banking system, such as by examining credit shortages and assessing how an alternative banking arrangement could be more equitable and sustainable. In some cases, the negative results of feasibility studies prevent public banking efforts from moving forward. For instance, in 2011, the state of Massachusetts commissioned a feasibility study of the Federal Reserve Bank of Boston that concluded the Bank of North Dakota model was inapplicable to Massachusetts.⁷⁵ In other

74 <https://www.publicbankinginstitute.org/legislation-local-groups-by-state/>.

75 Kodrzycki and Elmatad, "The Bank of North Dakota."

states, such as in Vermont and Maine, legislatures were unwilling to endorse public banking regardless of the positive results of feasibility analyses.⁷⁶

Among the initiatives for creating a public bank along the lines of BND, two efforts from Oregon and Washington produced positive outcomes, even though the results did not allow for a stand-alone deposit-taking institution. Oregon instituted a Growth Board that consolidated existing funds and programs for venture capital loans to seed start-ups.⁷⁷ Washington introduced two pieces of legislation, HB 2434 and SB 5464, establishing the Washington Investment Trust, which is expected to serve as a depository for state money and facilitate investment in infrastructure development programs.

With some exceptions, most notably in California, public banking is not nearly close enough to being put into practice. Despite operating in an antagonistic political climate, the public banking movement continues to build boundary-spanning networks, discuss and popularize new possibilities, and sustain independent discourse.⁷⁸ CPBA, Demos, and PBI continue to work with activist groups to support legislation in various states. Rocky Mountain Public Banking Institute, Mass Public Banking, Public Bank NYC, and Portland Public Banking Alliance are among the examples of boundary-spanning public banking advocacy groups.

While many of these initiatives are operating at the local or state level, some initiatives are designed to operate on a larger

76 Deborah M. Figart and Mariam Majd, "The Public Bank Movement: A Response to Local Economic Development and Infrastructure Needs in Three U.S. States," *Challenge* 59, no. 6 (November 2016): 461-79, doi.org/10.1080/05775132.2016.1239962.

77 Schneiberg, "Lost in Transposition."

78 Schneiberg, "Lost in Transposition."

scale.⁷⁹ One proposal calls for a green bank seeded with capital from the US Treasury and supported by loan guarantees and short-term financing from the Federal Reserve. Other ideas include a public investment bank that will incentivize the investment of private capital into green financing.⁸⁰

In addition, PB&F initiatives are necessary to finance patient capital into long-term investments in human capital and technological innovation for “high road” jobs. Such attempts include the IBank initiative in California, a national investment authority,⁸¹ and the resurrection of the Reconstruction Finance Corporation.

The role of the Federal Reserve is crucial in these initiatives. Successful large-scale PBFs, like their private and for-profit counterparts, need to be backed by a bankers’ bank with short-term financing, support during periods of financial crisis, and financial guarantees. The Fed fulfills these needs for US banks. Expanding its purview to include supporting PBFs or creating a new institution to provide this support would be critical for the success of PB&F institutions.

As an illustration of this range of PB&F solutions, Table 1 presents a taxonomy of PBFs. Table 1 identifies a variety of institutional solutions that include public, private, and public-private forms of ownership, as well as small, large, centralized, regional, and local institutions.

79 For financing for a Green New Deal, see: Marois, “Towards a Green Public Bank”; Robert Pollin, *Greening the Global Economy* (Cambridge: MIT Press, 2015).

80 Hockett and Omarova, “Private Wealth and Public Goods.”

81 Hockett and Omarova, “Private Wealth and Public Goods.”

Table 1. Public Banking and Finance Institutions (Examples)

Source: Authors' rendering

ROLE	FUNCTIONS	OWNERSHIP STRUCTURE
Payment Mechanisms	Effectuate payments efficiently and cheaply	<p>PUBLICLY OWNED</p> <p>Postal savings bank, Federal Reserve accounts</p> <p>PUBLICLY ORIENTED NOT-FOR-PROFIT</p> <p>Cooperative or nonprofit digital money mechanisms</p> <p>PUBLIC-PRIVATE PARTNERSHIP</p> <p>Current banking system</p>
Short-term credits for the working class and the poor	Access to funds for emergencies, income spending mismatches, etc.	Cooperative banks, credit unions
Long-term credit mobilization and allocation, employment creation	Provide long-term credit for human and physical capital investments and innovations	<p>Postal savings banks, state public banks, municipal banks</p> <p>Reconstruction Finance Corporation, national development bank, national infrastructure bank</p> <p>Nonprofit, socially responsible investment funds with government support</p>
Wholesale finance, insurance provision, other finance facilities	Provide financial infrastructure to undergird publicly oriented financial system	Public banks (e.g., Bank of North Dakota), public credit rating agencies, democratized Federal Reserve
Specialized Finance	Provide needed credit (and equity positions) for long-term critical social needs	

Climate change	Provide investments, underwriting, lines of credit, and guarantees in the development, consumption, and production of green energy	Green banks, green investment funds	Nonprofit green investment funds, socially oriented asset management funds	Public support for private funds that invest in renewable, green energy
Financial inclusion, community development, poverty reduction, housing	Comprehensive financial and investment plans, land transfer and housing	21st Century Homestead Act, local public banks, municipal banks, state public banks, postal savings banks	Community development credit unions, CDFIs, community development funds and public supports such as subsidies and financial infrastructure	Community development banks with private investment component (Minsky's proposal for a network of community banks with a public bankers' bank as facilitating institution)
Cooperative and socially oriented financial support	Provide support to cooperative enterprises and financial institutions that are socially oriented	Cooperative banking fund		
Education	Provide financial support for students and educational institutions	Public education fund for students and public educational institutions, debt cancellation and forgiveness facilities		
Housing	Provide affordable housing at federal, state, and local levels	Public housing financing banks and authorities; Federal Reserve financing of affordable housing		

Models of Public Banking in the United States and the Challenges They Face

For PBFIs to thrive in the long term, they have to be sustainable. Like private banks, PBFIs cannot continually run deficits and expect to survive unless they have a source of outside funds. This raises a question about limits on the banks' ability to achieve their social goals while remaining financially intact.

As we discussed in the previous section, PBFIs have certain advantages over private finance that allow them to compete. However, we cannot expect PBFIs to achieve their missions in a capitalist economy like the United States unless they receive the same kind of support that private banking does. If they were to receive even a fraction of the support that private finance gets from the government, they would generate significant benefits for society.

Public banks face several notable imperatives, constraints, and challenges, just as private banks do. They must raise funds to initiate their operations; they must not routinely lose money on their loans and investments; they must not become vulnerable to liquidity crises and bank runs; they must control the expenses they incur to locate, screen, and monitor their loan customers; and they must avoid fraud and corrupt practices on the part of managers and directors.

Thus, public banking and finance institutions face the following risks: funding risks, credit risks, liquidity risks, and corruption risks. These have to be managed properly if PBFIs are to sustain themselves and serve their public missions.

Funding Risks

One of the main challenges public banking organizations face is securing funds. These institutions can fund themselves by i) appropriation of public funds from the federal, state, or municipal budget, ii) bond issuing, and iii) the sale of bank stocks.

Take the example of a state-level or municipal public bank. The funds needed for capitalizing a state bank can come from pension funds, local governments, or the state government, either through bond issuing, repurposing “rainy day funds,” or tax revenue. Most public banking initiatives consider a mix of approaches to meet capitalization requirements. Bond issuing has a political advantage because it avoids lengthy negotiations over the state or municipal budget. But the challenge is that it requires building enough trust in advocates’ proposals that agencies and private investors will be comfortable participating in bond purchases and depositing their funds in public banks.

Another approach involves appropriating funds set aside for the purposes a public bank could serve. We dub this the “consolidation approach,” as it requires consolidating preexisting authorities into a public bank. For instance, advocates in West Virginia proposes consolidating four different agencies that currently operate independently of one another to provide loans and investment options to citizens of Virginia into the Bank of West Virginia.⁸² Advocates believe that by consolidating these agencies into a public bank that will have access to lines of credit from the Fed, they can eliminate inefficiencies and provide cheaper loans. Proposals to establish a state-level public bank in California similarly rely on a preexisting agency, the IBank.

Community development financial institutions (CDFIs) are another example.⁸³ The three levels of government make up 37 percent of the total financial resources of CDFIs. Local governments

82 <https://www.bankofvirginiaact.org/about.html>

83 This draws on Clifford N. Rosenthal, *Democratizing Finance: Origins of the Community Development Financial Institutions Movement*, (Victoria, BC: Friesen Press, 2018); and Brent C. Smith, “The Sources and Uses of Funds for Community Development Financial Institutions: The Role of the Nonprofit Intermediary,” *Non-profit and Voluntary Sector Quarterly* 37, no. 1 (March 2008): 19–38.

provide funds through their involvement in local business development and housing provision. They further support CDFIs through tax incentives and government-sponsored small-business training programs. State government agencies, such as housing authorities and commerce departments, strategically employ CDFIs as a local policy-implementing agent to administer and distribute public capital. Finally, at the federal level, there is an entity in the US Treasury Department, the CDFI Fund, set up to enable CDFIs to build their balance sheets, make their own lending and investment decisions, and leverage private-sector support. Business development loan funds (BDLFs), another type of CDFI, are tasked with lending capital to businesses and nonprofit organizations that do not typically qualify for funding from traditional sources. They obtain capital in the form of grants and below-market-rate loans from federal and state governments, banks, and philanthropies, which they then relend at market rates, using the difference to finance their operations. Community development venture capital (CDVC) is another form of CDFI that provides equity capital to small businesses. CDVC funds come from banks, foundations, and state and federal governments, which invest in low-interest debt or equity for periods of ten or more years.

Liquidity Risks⁸⁴

All deposit-based financial intermediaries are subject to liquidity risk: the bank runs portrayed in classic movies *It's a Wonderful Life* and *Mary Poppins* show vivid Hollywood renditions of this dry technical term. PBFIs can maintain sufficient liquidity by keeping

84 This section draws on Sebastian Leder Macek, "Public Banking in the Northeast and Midwest States," The Northeast-Midwest Institute, September 2019, nemw.org/wp-content/uploads/2019/09/Public-Banking-White-Paper.pdf; Karl Beitel, "Municipal Banking: An Overview," Roosevelt Institute, 2016; Karl Beitel, "The Municipal Bank: Compliance, Capitalization, Liquidity, and Risk," Roosevelt Institute, 2016.

a portfolio that is not highly speculative and that has a buffer of liquid assets such as US government securities; by establishing lines of credit with larger public financial sources such as the state, the Federal Reserve, or the Federal Home Loan Bank Board; by gaining access to deposit insurance; and by having a stable deposit base — often represented, in the case of municipal or state banks, by payroll and tax deposits from the state or municipality that operate on a predictable schedule.

Credit Risks

A rigorous loan approval process and knowledge of borrowers is key to managing credit risks. Smaller, geographically concentrated PBFIs may incur extra risk from geographically concentrated credit shocks. But having access to networks of public banks or other financial institutions that will allow PBFIs to sell off some or all of their illiquid and large loans can help them manage highly concentrated risks.

Corruption Risks

A final potential risk facing PBFIs is the undermining or perversion of their activities by financial officers of bank boards that attempt to defraud or corrupt the bank — or, more subtly, increase the bank's returns by lending credit or buying assets that might have higher returns but that are not consistent with the mission of the institution, or that might be excessively speculative and risky. The solution is to have broad-based, democratic input into the operation these institutions, strong technical management, as well as monitoring by appropriate national, state, and local authorities.

Challenges

Technical expertise in the development of PB&F initiatives can be a challenge. For example, our interviews with public banking

organizers informed us that organizations sometimes find it challenging to maintain control over the quality of feasibility studies due to lack of financial resources. Given that public banking advocacy is largely built on voluntary efforts, suffering from a lack of financial resources and shortcomings in some operational capabilities is to be expected. To succeed, funding and technical infrastructure for activists promoting PB&F must increase significantly. Private foundations are one source of funding, but they are often quite flighty, subject to fad and fashion. There is no substitute for the investment of federal, state, and local government funds, for the design and development of public banking and finance.

Several advocates we interviewed stressed that one of their biggest problems is the lack of understanding of public banking. Many people find money and banking intimidating subjects to be left to experts — a problem further aggravated by the lack of familiarity with the concept of public banking in the United States. Building support to pass legislation in more states will require educating the population and interest groups about how an alternative PB&F system could work.

Finally, the power of market-oriented interest groups in framing debates and influencing policy-making presents significant challenges to public banking initiatives.⁸⁵ As such, public banking needs to be supported by a broad-based movement that would contest the neoliberal paradigm and overcome political gridlock by replacing incumbents who are hostile to PBFIs.

IV. CONCLUSION

The financial infrastructure of the United States is not appropriate for addressing the massive challenges we face — far from it. Despite having the most “advanced” private financial system in the

85 Schneiberg, “Lost in Transposition.”

world; being home to megabanks, the dominant asset managers, and management companies;⁸⁶ and being the center of shadow banking institutions and the premier central bank and currency on the planet, the United States finds itself with a financial system that ignores the needs of its communities, its businesses, and the planet.⁸⁷ Even worse, it requires multitrillion-dollar bailouts by the public on an increasingly frequent basis, while generating extraordinary riches for its management and creditors despite its abject failures.

In other countries, there has been a resurgence of public-oriented banking as the challenges facing their economies and the failures of the private financial institutions mount. But in the United States, apart from the public bailouts that have effectively “nationalized” some of the financial institutions, including government-sponsored enterprises (GSEs) like Freddie Mac and Fannie Mae, public banking and finance has remained small and underfunded. Why?

The answer is the opposition of the private banking system, their political friends, and the public financial governance institutions that favor private banking — most importantly, the Federal Reserve. The story of public banking after the GFC tells the tale. In response to the failures of finance and the enrichment of private bankers at the public trough, more than thirty proposals for state and municipal public banks were developed and pushed forward.⁸⁸ But, with the exception of California and possibly New Jersey, none of these initiatives have come to fruition. In Massachusetts, the Federal Reserve’s opposition was quite explicit: it reviewed the

86 Gerald Epstein, “The Asset Management Industry in the United States,” PERI Working Paper, 2019, peri.umass.edu/publication/item/1243-the-asset-management-industry-in-the-united-states.

87 Epstein and Montecino, “Overcharged.”

88 Schneiberg, “Lost in Transposition,” 285.

proposal for a state bank and pronounced that it was unnecessary and would be unsuccessful. Bills in other states met similar fates.

This opposition came about even though those framing these proposals were careful to follow the Bank of North Dakota model of partnership banks that would not compete with private banks at all. But the danger of risking future competition was too great for private-bank-friendly politicians to stomach. The general anti-government ideology prevalent in the United States likely also played a role.⁸⁹

The risk is that, as activism for public banking and finance regenerates, the same ideological counterforces will squash it once again. Preventing that from happening and continuing to build a substantial and effective public banking and finance system in the United States will require not only continued grassroots efforts but also strong efforts at all levels of political organizing.

Institutionally speaking, what is needed to foster PB&F on a scale that can truly address the challenges we have discussed here is for the premier public financial institutions in the United States, including the Federal Reserve, the US Treasury, and the Federal Home Loan Bank Board, to step up and provide the infrastructure supports for PBFIs that they do for private finance. This means supplying liquidity facilities, seed capital, loan guarantees, equity investment partnerships, technical support, and emergency backup. Without this financial infrastructure, PB&F will be at a disadvantage relative to private finance and will not be able to provide the public options that will make it more efficient, more socially responsible, and competitive.

In the last two economic crises, the Federal Reserve has shown that it has the capacity to provide financial facilities outside its typical modes of action. In the current COVID-19 crisis, the Fed

89 Schneiberg, "Lost in Transposition," 303.

has created multiple structures to prop up the financial system as usual, as well as a few that are designed to provide funds to medium-size businesses and state and local governments. Yet the Fed has failed to design these facilities in a way that can genuinely offer broad assistance.⁹⁰ For example, the Fed has a capacity to spend \$450 billion for state and local finance, but it has spent only \$14 billion in that arena. Meanwhile, it has spent many billions of dollars to prop up asset markets, including corporate junk bonds.

It's clear that there is more the Federal Reserve can do in this respect. Just as it did during World War II, the Fed can first implement and then expand its facilities to help support the creation and expansion of PBFIs. At the national level, it can support critical initiatives like a green bank, a postal savings bank, and Fed accounts. Regional Federal Reserve Banks, in turn, can play a larger role in supporting regional, state, and local PBFIs, including creating state and municipal banks and infrastructure finance banks.⁹¹

The last decade has made it obvious that the problems we face are growing, and that the likelihood our bloated private financial system can help solve them is shrinking. We have to think as big as the problems confronting us. Building public banks is critical for our future. Now we must work at the national level to make sure existing public financial institutions support these efforts, rather than standing in the way, as they have done for so long. ☞

90 Gerald Epstein, "Human Capital Bonds and Federal Reserve Support for Public Education," *Just Money*, 2020. justmoney.org/g-epstein-human-capital-bonds-and-federal-reserve-support-for-public-education-the-public-education-emergency-finance-facility-peeфф/.

91 See, for example, Epstein, "Human Capital Bonds"; and Gerald Epstein, "Reforming the Federal Reserve for the 21st Century," in Gerald Epstein, *The Political Economy of Central Banking: Contested Control and the Power of Finance* (Elgar Press, 2019), Chapter 23.