Public Banking: A Community Based Banking Solution for Sonoma County

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Abstract:

The privatized banking system in the United States often exploits and robs citizens of personal and public funds through risky investments, contractual obligations, and generic fees. It was these risky, profit maximizing practices which were largely responsible for the 2008 financial recession and while the banks could have been held accountable, they were instead bailed out with public funds with no obligation to give back to the communities which had supported them and without any plans to prevent similar economic catastrophes. In this paper, we review the current economic system of the United States, how public banking can supplement and improve the current system, and how public banking can benefit Sonoma County specifically. Our group of 8 Sonoma State Undergraduates reviewed studies published both at home and abroad, and conducted interviews on the pros and cons of a public banking system with leaders and activists in the field like Ellen Brown, Deborah Hammond, and Shelly Browning. For perspective from community banking level, an interview was also conducted with Robert Eyler, a member of the board of the directors of Redwood Credit Union. The results of our study reveal that the monopolization of the private banking system exploits citizens, small business, and communities, and stifles communal growth via loan programs designed to earn maximum profits for investors in Wall Street regardless of the negative impact at the local level. Public banking appears to be a viable solution to these problems and through partnerships with local and communal banks can provide many of the same services of the private industry but at lower costs and at the will and the benefit of local communities.

Introduction:

Like most developed countries in the world, the economic policies of the United States are based almost entirely in debt to GDP ratios (Brown 2013). Using these concepts, wealthy organizations exploit the working class in order to maximize profits and support a capitalistic economy (Brown 2013). One of the primary methods of this exploitation occurs through the creation and distribution of debt. The problem with this system is that privatized banks, which control the vast majority of public funds, prioritize the use of that money to support shareholders rather than local and communal investment as the public might expect of their tax dollars. As a result, public funds can often be gambled through a process often referred to as "Shadow Banking" where private banks engage in lending practices outside our regulatory restrictions (Brown 2013).

While private banks are often engaged or caught in unethical business transactions, the public is limited in alternative options as a handful of private banks (Chase, Wells Fargo, Bank of America, Citigroup) have monopolized the U.S. banking system. Since the recession in 2008, discussion around the creation of a public bank has increased dramatically across the United States. A public bank is a state or city-owned banking alternative specifically designed and mandated to provide localized economic support and transparent investment opportunities. Public banks are rather prevalent throughout the world but aside from the Bank of North Dakota, are non-existent in the United States. With so little competition in the private sector, and so few options for consumers, would a public bank be a viable alternative for economic development in the United States? And if not on a national scale, what about the at the local or city level?

The Current Banking System:

In 2008 the United States entered a deep recession comparable only to the great depression of the 1930's. The vast majority of this recession was caused by risky, subprime mortgage lending which, while legal, placed both the economy, and the homes of American citizens at risk in favor of massive profits for large, private banks. When the financial sector was on the brink of collapse, the American government bailed out its major financial institutions with hundreds of billions of dollars of public funds. While almost entirely repaid, few regulations, if any, were put into place to ensure the privatized banking system did not put the public in jeopardy again.

Without new regulations and rules to prevent a similar collapse, there is no reason to expect the economy not to fail again (Brown 2013; Ruth 2014). The economy is heavily controlled by three powers; the government, big businesses, and Wall Street (Brown 2013). "Wall Street" is generally used as a metonym for various financial institutions which heavily influence the US market. Wall Street investment banks use their customers' deposits to gamble in the stock market while the government sets laws, regulations, and guidelines for a "free market" and overlooks violations and non reinforcement (Brown 2013; Tonveronachi 2013).

The process of bank globalization required a series of minimum standards to manage the competition between banks and national regulators. However, the big banks avoided some of the laws and regulations and took advantage of the "soft laws." Soft Laws are laws that are not strictly binding but have legal significance (Tonveronachi 2013). The failure of regulation on cross-border banks and their crises caused many jurisdictions to "ring fence" (when portions of company assets or profits are financially separate from an entity) national banking systems. Ring fencing was created to help shield public finances from bank crises. While "big name banks" took advantage of soft laws to become globalized, it later affected them during the 2008 banking

crises when they didn't have the necessary structure to survive a financial downfall. This all occurred because Wall Street banks gambled money they did not have via shadow banking and the government failed to regulate them in the wake of seemingly endless profits and American economic expansion (Brown 2013; Tonveroachi 2013; Ruth 2014; Grossman 2016).

Since World War Two, local governments all over the nation have made deals with private banks dependent upon derivatives, a financial tool which derives its value from another financial asset (Morgenson 2012). Private banks encouraged local governments to enter into such deals as well as interest-rate swaps as a way to save the public's money on their public works. Local governments essentially agreed to pay banks fixed-rate payments while the bank makes variable-rate payments to whomever they borrow money from. Initially, this was a great deal for local governments assuming rates stayed high. When interest rates dropped in response to the crisis of 2008, local governments have been stuck paying pre-crash interest rates while the banks pay next to nothing (Morgenson 2012). New York state alone has spent $243 million dollars of public funds in recent years to remove itself from swap-related debt, and a study done by the Refund Transit Coalition found that 1,100 swap deals among more than 100 government agencies are costing taxpayers roughly $2.5 billion dollars per year (Morgenson 2012). Local governments have been petitioning private banks to renegotiate contracts post-crash, but the banks are refusing to do so as they are under no legal obligation. This means the U.S. private banking system has no problem using public funds when they require a bailout to save their business, but the same banks have issues bailing the public out of contracts made during far more stable economic times (Morgenson 2012; Brown 2013).

Public Banking; An Alternative:

Public Banking can help the economy get back on track in the United States and particularly in California. Ruth (2014), discusses how California and other U.S. banks are in debt from borrowing money at high interest that are made difficult to pay. “We lost billions by paying their inflated interest rates… Money and access to credit help determine what kind of a society we live in, what our priorities are, and what our future looks like” (Ruth 2014). A bank that is owned by the public could prioritize investment in areas like infrastructure and city development rather than strictly profit based motives. Public banks can provide many of the same services that privately owned banks do, but without a profit motive, at a lower price and without participating in dealings that will cost the stakeholders, citizens, and companies their money, dwellings, and businesses (Brown 2013). Along with a safe and honest place to stash and invest money, public banks also help the local and nation’s economy (Brown 2013; Figart 2016; Goodman 2010). For example, public banks do not pocket profits but return profits back to investors (Figart 2016). If infrastructure is collapsing or schools need funds for programs then the bank’s profits will pour out into those places that need attention (Figart 2016; Sabatine 2017).

Profit is not inherently bad as a motive for business, but its priority must shift when the public good is at stake. Private banks argue that their loan programs for business owners and cities encourage economic growth but their profits and expansions are consistently siphoned from local communities straight into shareholder pockets. While a private bank’s loan might have helped build a new school, the excess public funds going towards interest alone could have easily been used on additional projects. Assuming the school was going to be built either way, it could be argued the profit from interest on the loan actually stifles the public sector as it is never reinvested into the area it was originally taken.

Beyond public works, there is growing argument for the necessity of localized public banks to operate as safe havens from discrepancies between state and federal law. The legalization of Marijuana in California has brought this issue to the forefront as Cannabis is still an all cash business due to its illegality at the federal level. By opening a public bank, the cannabis industry would have a place to make deposits thus providing opportunity to benefit the economy through taxation which would bring revenue to the state (Lybarger 2017). This cannabis boost to the economy would be followed by a decrease in cannabis crime as many growers and distributors have nowhere safe to store their cash and are often the targets of thieves and murderers. Allowing the cannabis industry to be a part of a public banking system would not only relieve fiscal distress and fix social ills, but would pave the way for the economic stimulation expected of the cannabis industry which can be attributed as a primary cause for its legalization in the first place (Lybarger 2017; Grossman 2016; Ruth 2014; Sabatine 2017).

Public banking can lead to lower interests rates, a resilient economy, low inflation and unemployment, consistent economic growth, financial cushions for hard times, solutions to poverty, and community self-sufficiency (Brown 2013; Figart 2016; Grossman 2016). These effects can be seen in places that have public banks such as Brazil, Russia, India, China, South Africa and the Bank of North Dakota in the United States (Brown 2013; Figart 2016). Last year China unveiled their “belt and road” initiative which pledged one trillion dollars to an infrastructure venture which would link China to Europe with a new silk road. Upon its projected completion in 2049, the new trade route could allow China to become the wealthiest nation in the world. How is China able to raise so much money for one project? Almost entirely by loaning themselves the money at low interest rates through the country’s five largest banks, which are majority-owned by the federal government (Brown 2018).

Doug McKenty, the author of “The Timing is Right for Public Baking,” interviewed Ellen Brown and Walt McRee about what’s going wrong with the current banking and economic system and how public banking can be the solution (2017). McRee states ,“The predicament that we’re in is unsustainable because you can not borrow yourself out of debt but we assume [debt just as a fish assumes water.] We are stuck in the system [that] is crashing and it's taking us with them” (McKenty 2017; Miller 1998).

California has faced one budget crisis after another for the last three years from the, “constrained private credit conditions, unemployment levels well above the national average, and the stagnation of state and local tax receipts” (Brown 2013). However, this is not the case for the Bank of North Dakota (BND) which was the first state owned bank that found its own solution to banking by uniquely acquiring money (Brown 2013; Rose 2012). The BND partners with community banks to provide loans using the state’s assets. Profits from interest paid on these loans go back to the state and community banks rather than the shareholders of private banks.

Privately owned banks want to make as much money as possible while publicly owned banks are mandated to grow the local economy . As a result, public banks would offer loans at rates as low as possible since the goal is communal growth rather than profit (Rose 2012; Brown 2013; Tonveronachi 2013; Miller 1998). If California followed North Dakota and started its own state bank they could also reap the benefit of cheaper infrastructure projects. A prime example is the San Francisco Bay Bridge. The initial loan for the project was 6.4 billion dollars, but after 20 years of interest payments, California tax payers are expected to pay roughly 13 billion dollars (Tasini 2017). For taxpayers to pay nearly double the cost of a project is not only an extremely inefficient use of public funds, it raises several ethical concerns on the practice of profiting off taxpayer dollars.

Since 2008 over twenty other states have passed bills to investigate the feasibility of establishing a public bank. Cara Lombardo, an editorial intern for *The Progressive* wrote an article exploring the resistance public banking received from The Federal Reserve Bank of Boston which deemed public banking as unnecessary. Most of the pushback towards public banks is due to "the political influence of large banks [which have] sabotaged or limited many proposals" (McKenty 2017). They question the feasibility of public banks and oppose giving states the ability to gamble tax dollars. The BND was one of the only banks to successfully weather the 2008 recession because they never engaged in subprime lending. In fact, the BND has had a larger return on investment every year for the past 12 years (Brown 2016). The opposition also claims that a public bank would create too much competition for private banks, which there is no evidence of. Public banks do not necessarily have to compete with privately owned banks, but partner with local banks to provide low-interest loans to small businesses and infrastructure projects (Brown 2013; Lombardo 2016; Bichsel 2006).

Benefits to Sonoma County

Approaching public banking from a local level doesn't always have to be about economic development. Sometimes tragedy strikes and funds are needed to rebuild. From 2015 through 2017, Sonoma County has experienced a spree of devastating fires. The most recent, in 2017, was especially destructive as it destroyed over 8,400 homes and dealt nearly a billion dollars worth of damage. Private banks have no incentive to assist in rebuilding communities, and even if loans are offered, the rates are still aimed at profit rather than public development. A publicly-

owned bank could benefit Sonoma County by stimulating growth when privately-owned banks fail to do so (Swearingen 2012; Brown 2013; Ruth 2014).

Public banks can reduce the cost of infrastructure by providing loans to the government at lower interest rates and reinvesting profits back into the community, rather than distributing them to out-of-state shareholders (Swearingen 2012). Public banking would be able to financially help all residents in the county. Those individuals who lost homes would have lower interest rates on home mortgages because public banks will be able to charge less than big banks (Brown 2013; Grossman 2016) and the profits from those low-interest rate loans will cycle back to the community in order to promote economic growth (Brown 2013). Public banking would also be able to provide larger budgets for support programs that help with mental health, physical health, homelessness, and suicide (Brown 2013; Digitale 2018). Because public banking leads to lower interests rates, a resilient economy, low inflation and unemployment, consistent economic growth, financial cushions for hard times, solutions to poverty, and community self-sufficiency, there will be an all around quality of life improvement in Sonoma County (Brown 2013; Figart 2016; Grossman 2016).

Research Question:

How would Sonoma County Benefit from a Public Bank?

Research Method

Interview three public banking advocates/ activists

- Debora Hammond
- Shelly Browning
- Ellen Brown
- Francisco Herrera

Interview one banking expert

- Robert Eyler

Surveys

- 86 participants from public banking presentation and social media avenues

Interview Findings:

To gain a better understanding of the pros and cons of public banking, and the difficulties faced in implementing the system, we interviewed Ellen Brown, Shelly Browning, Robert Eyler, Francisco Herrera and Deborah Hammond. Ellen Brown is an author and leader in the national public banking movement who provided valuable insight into the advantages of the system and the challenges the movement faces. Shelly Browning and Deborah Hammond are local activists fighting for the creation of a public bank in Sonoma County and had intimate knowledge of challenges faced at the local level. Francisco Herrera is a community activist who ran for Mayor of San Francisco in 2015 on the Green Party ticket who promoted a public banking initiative during his campaign. Robert Eyler is a professor of Economics at Sonoma state and a member of the board of directors of Redwood Credit Union. Mr. Eyler provided information on how public banking is viewed from a community banking standpoint.

After interviewing Deborah Hammond and Shelly Browning, we learned that public banking for Sonoma County is not feasible with just the city of Santa Rosa itself due to small size and volume of its population. As a result, Santa Rosa is partnering with Eureka, another charter city in the neighboring Humboldt County, to open public banks in the form of a municipal bank. As charter cities, both Santa Rosa and Eureka have more flexibility in economic policy and are currently discussing the feasibility of sharing a public bank between them.

According to Hammond and Browning, a public bank was proposed in 2011 but Jerry Brown (Governor of California) pocket vetoed the legislation citing failed feasibility studies and an ever increasing problem of unbalanced California budgets. As a result, cities are focusing on public banking at a more local level. In efforts to start public banks in these cities, feasibility studies are being conducted to see how public banking will help the community and where the cities' money will be invested. For example, Sante Fe has completed their feasibility study, however lack of public education and financial literacy have delayed the start of public banking even though the city had more than enough money (60 million dollars) to start a public bank. Another reason public banking has been delayed in start up and popularity is because the money that would be used to start and maintain public banking is being used to pay off debts to private banks.

Public banking could benefit and help support surrounding and contributing communities and regions by assisting in tragedy recovery, infrastructure maintenance, etc. For example, the Golden gate maintenance repair would have cost 6 million dollars if California had its own bank, but because California banks with private banks, interest rates at 4-6 percent hiked up the price of maintenance to 12 million dollars. The increase in interest rates which result in higher prices are also due to the need for more taxes to cover the cost of infrastructure and city revenues after tragedy has occurred or maintenance is needed.

Public banking is also on hold because Santa Rosa's city income relies heavily on the homeowner property tax. The loss of homes due to the fires in Santa Rosa cut 17% of the cities revenue, a significant amount. As the city loses money, it becomes more and more difficult to allocate the funds for creating an entirely new financial institution. The ironic side to these

difficulties is that having a public bank to begin with could have balanced the financial hit Santa Rosa took.

Hammond and Browning's discussion wasn't only about public banking however. Banking, in general, can be difficult to understand for the public because the banking system is very complex and has a high command of the English language and low command in layman's terms. This means that every day citizens who do not spend much time thinking about banking or economics may lack the knowledge necessary to make decisions on the matter. This is important because if people do not know about how banking works then they will not understand how public banking would be any different. Some of the basic things a citizen needs to know is the difference between a shareholder and stakeholder, where profits from loans are being invested, how is debt created and distributed, and how debt/ loans/ banking impacts the community, state, nation, and world both negatively and positively. For example, in the current banking system, the government does not create the money supply, the banks do. This gives banks the freedom to create as much money in the form of debt they want which affects cities negatively because the cycle of constant debt is established through banks giving loans to the city and charging high interest rates along with hundreds of thousands of dollars in fees just for banking with them. An example of this is Santa Rosa not only taking loans from Wells Fargo, but having to pay $350,000 dollars per year in fees to just to bank with them.

Wells Fargo, a commonly selected choice when cities need loans, was demoted to "needs improvement" status according to the Department of Justice, which means they are an unsafe institution to bank with. However, Santa Rosa is still banking with them and a few other banks as city activists and bankers conduct a feasibility on Santa Rosa and Eureka in partnership with public banking. The reason Wells Fargo is still being allowed to bank with the city is because of

the bidding process where cities decide what bank to contract with for a certain amount of time and when the contract is over the city is free to choose the bank they would prefer or bid the highest. In Santa Rosa's latest bidding session, the city decided to bank with a foreign bank, a local bank, and Wells Fargo because the previously listed banks were too small to handle the city's volume of funds and that is what sections of Santa Rosa's citizens wanted. As of now, public banking activists are asking the city to contract with these banks for a year so when the feasibility study is completed and shows that public banking is beneficial, the city can bank with a public bank instead of the privately owned banks that create cycles if debt through expensive banking fees and high interests rates.

Although public banking shows promising benefits to the community, region, and state, it is not a cure all to current economic crisis or social ills. Public banking will supplement the current system instead of completely fixing it. For example, public banks may not be able to reduce state and federal taxes immediately, but by using the low to no interest funds on infrastructure projects will save the public in the long run. Public banking is also needed to protect the economy from President Trump's dismissal of banking restrictions, such as the repeal of the Glass-Steagall Act which means banks are under the same regulations and laws that resulted in the 2008 economy collapse and recession. In order to start public banking, the younger generations need to be educated about the movement to keep the momentum going.

The feasibility of public banking has been hotly debated since the recession. Advocates claim that there should be publicly owned banks because they would be able to provide loans without a profit motive. Critics ask why the country needs another financial intermediary providing loans? How will a public bank keep the lights on if they only loan at low interest rates? Why would any municipalities want to gamble their tax funds? If California wanted to start a

state-owned bank, where would they get the money? Some have suggested that the state could use CalPERS funds to get a public bank up and running, or the money would come from tax money. A public bank would receive that tax money from local and city taxes and invest in the public bank start up. Another option would be to get the start up money from retirement savings. Although the options have been discussed, the issue is still being speculated because it would be difficult to convince the public to allow politicians to risk their pensions.

The Bank of North Dakota brought more support to public banking once analysts realized North Dakota was the only state to have a budget surplus every year since 2008 (Brown 2013). The BND operates by partnering with local banks and credit unions to provide loans to farmers and small businesses. Dr. Robert Eyler, who serves on the board of directors for Redwood Credit Union, thinks North Dakota's model could work in California, but he says the rest of the directors aren't sold on the idea of partnering with a public bank. They are concerned about which municipality would be running the bank and how stable that municipality is.

In the interview with Ellen Brown, she shed some light on how Los Angeles spends more money on bank fees than they do on infrastructure. We learned that the bank of North Dakota applies a mere 2% interest rate on infrastructure loans while Wall Street banks ask for double, around 4 to 5%. This is important because these high rates for the same project allows for cities and businesses to be involved with the cycle of debt that they have to pay significant amounts of money to the bank for. In addition, insuring a public bank is still an aspect that would need to be carved out as the rules aren't set up for a public banking system. Ellen stressed the need to get public banking right the first time by giving the people an idea oh how it will be ran and showing them they will have access to all the information they want to know about their money compared to the way wall street banks have kept everything a secret. When asked how we can trust the

state government to run a bank, the conclusion was that public banks are trustworthy and safe from corruption because routine audits would take place and there would be little incentive, such as bonuses, commissions, or gambling of money, that would allow for corruption by the hands of public banking employees or politicians. These audits would also be accessible to the public to allow complete transparency for public banking business handling, unlike private banks, along with unbiased voting and employment of people that hold community advancement at a high priority.

Francisco Herrera, a community activist who is a strong advocate for public banking, believes that it's important to have people control of the budgets that directly affect their home. Herrera states that by having in more direct control of local funds, then the people will have the incentive and the power to keep their community affordable. Herrera also believes that the way to get things rolling on starting a public bank in a city like San Francisco is to bring together several community banks to help in the process of creating a public bank. Herrera states that when the money is in the control of the people, then the people can really start thinking concretely about what they need as a community and get to decide what to do with their money. Herrera also brings up an important point about having public control over public funds. By providing a more direct route for people to dictate where funds could be best used, Herrera believes interest in the democratic process will grow thus contributing to a stronger government and more confident communities.

Data collection from surveys:

Surveys were conducted during Social Justice week at the end of the Public Banking presentation and via a Google form created to obtain more responses from the community about the knowledge of Public Banking. The data shows the responses from both the surveys taken in

person and online from participants from social media such as facebook, instagram, and twitter as well as the use of text messages and email to receive as much data on random people's public banking knowledge as possible. Although the surveys do not include any demographic information such as age, gender, and race, the data reflect there is a high need for education on public banking because majority of people do not know what public banking is, how it works, how it is beneficial, or where public banking advocates could receive more support.

Our data collection shows out of 86 people who participated in the survey only 23 participates had a vague idea of what Public banking was. The remaining 63 had no knowledge of Public Banking, and of those who were educated about public banking 47 believed that public banking would either possibly, maybe or could be beneficial for the community. 63.5 percent shared an interest in learning more about Public Banking, while 30.6 percent mention they would may be interested in learning more about Public Banking. 5.9 percent didn't share an interested in learning about Public Banking and 25 out of 86 participants didn't know if Public Banking could benefit the community. Only 5 participants believed that public banking would not benefit the community. 60 percent of our participants had a corporate bank, 10.6 percent had a community, 20 percent had both. 50 of the participants banked at 3 corporate banks; Bank of America, Chase and Wells Fargo.

The survey did not represent the general population, but represents a portion of what the Sonoma County community knowledge of Public Banking. From these surveys, we can conclude that there needs to be more resources for people to engage with to better understand and learn about the different banking solutions, such as public banking. This data could potentially be helpful to spark people interested in learning who to bank with now, and ask themselves why they chose the bank they have.

Conclusion:

Public banking could be a viable and effective alternative to the privatized banking system currently monopolizing American economics. The challenge with its implementation has less to do with the effectiveness of public banking, and more to do with how deeply the American economy is entrenched in an entirely privatized system. The concept of a public bank also raises questions about the ethics of private institutions making a profit on public funds. This is especially important when considering the reported costs versus the actual costs of projects like the new Bay Bridge where profit motivated interest nearly doubles the cost of the bridge over the course of twenty years. With a monopolized private system focused on profits made on interest based debt, most local communities and states have little to no opportunity to begin works on a public system before resolving the debt already owed to private institutions. Considering the 2.5 billion dollars spent annually by Americans on the interest for their public works, it is clear there is room for competition against these private banks profiting off tax dollars

Unfortunately for most cities, they do not seem to possess enough capital to create and run their own individual public banks. Their difficulties stem largely from the cycle of debt they're already struggling to pull out of. There are, however, some cities perfectly capable of creating a public banking system. Los Angeles and San Francisco are perfect examples of cities whose position as major economic powerhouses could set an example for the rest of the state and perhaps, the rest of the nation. Anyone interested in the topic of public banking certainly has their eyes on Los Angeles. The public banking movement in the region has picked up steam at

the same time that the city decided to look elsewhere for their banking needs after Wells Fargo was demoted to a, “needs improvement,” status.

Like any addition to the public sector, the first step in creating a public bank whether it be state or city run, would be to generate the support of voters. Most of the pressures preventing the creation of public banks come from the private sector lobbying to ensure the subject never even reaches the ballots. Even this lobbying pressure is almost non-existent as the majority of Americans are most likely unaware of the alternatives to private banking being proposed. One would expect the lobbying to increase as public knowledge and pressure increases, but the first step beyond feasibility studies, would be to raise public awareness of the issue.

Perhaps the most important thing about a push for a public banking system, is the conversation it ignites about economics, politics, and community. The feasibility studies being conducted in cities across the country might find public banking to be out of reach of certain communities, but the research itself is vastly important as it sheds light on the American economic system as a whole. While lawmakers have done almost nothing to curb the corruption and monopolization of a private banking industry which has repeatedly jeopardized the American public, it is clear that positive change can be made at a local level. Like our interviews, it all begins with a discussion about what can be done differently.

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Robert Eyler Information:

Link to audio: https://www.youtube.com/watch?v=AY2-9AYR6I4&t=109s

Francisco Herrera Information:

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