Washington Readies Sea Change for Wall Street; Rescue Plan Grows to $700 Billion; Similar Measures Urged Overseas

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The Bush administration yesterday raised the price tag on its emergency plan to revive the U.S. financial system, asking Congress for authority to spend up to $700 billion to relieve crippled financial institutions of their mortgage-based assets, an investment that would exceed the current cost of the Iraq war.

Senior administration officials meanwhile pressed their counterparts in Japan, Germany, Britain and elsewhere to establish similar programs to rescue their own troubled firms in what would be an unprecedented bailout of the worldwide financial system. The move comes in recognition that complex interconnections among financial institutions have created a global crisis that the United States cannot solve alone.

Congressional leaders responded positively to the administration's rescue plan, though the price tag was $200 billion higher than they had been told to expect just three days ago. But House Democrats said they would push to include a number of contentious provisions that could make it difficult to pass the plan quickly, including limits on executive compensation for firms that unload their bad assets on the government and new powers for bankruptcy judges to modify mortgages on primary residences.

Democrats also want President Bush to drop his opposition to a second round of federal spending aimed at stimulating the economy. While the administration's bailout plan would insure the money market funds of millions of ordinary Americans and help prop up the mortgage market, some Democrats worry that it will primarily be viewed as a bailout for big Wall Street firms.

"Obviously, this is of direct benefit to some people in the financial industry," Rep. Barney Frank (D-Mass.), chairman of the House Financial Services Committee, said of the rescue plan. "We need to be talking about direct benefits to people who are not in the private sector."

Bush, speaking to reporters during a White House appearance with Colombian President Alvaro Uribe, urged Democrats to set aside those demands. In talks with congressional leaders, Bush said he "found a common understanding of how severe the problem is" and the need for urgent action. "We need to get this done quickly and, you know, the cleaner the better," he said.

Bush also defended the size of the request, saying drastic action was needed because of the magnitude of the financial crisis, a cataclysm that started with nontraditional mortgage loans to U.S. homeowners, spread to the banking and financial services industry and now is enveloping markets around the world.

"This is a big package because it's a big problem," Bush said. "The risk of doing nothing far outweighs the risk of the package."

Bush, who campaigned as the nation's first MBA president and a free-market advocate, also appeared to address complaints from conservatives that the plan inserts the government too much into the economy.

"I'm sure there are some of my friends out there that are saying, 'I thought this guy was a market guy, what happened to him?' " Bush said. "My first instinct was to let the market work, until I realized, upon being briefed by the experts, how significant this problem became."

The proposal itself is just three pages long. But it lays out the most sweeping government intervention in the private sector since the Great Depression. In addition to $700 billion, the plan seeks vast new powers for the Treasury secretary to purchase mortgage-based assets from U.S.-based financial institutions over the next two years, to hire people to manage that portfolio and to issue regulations to stabilize the mortgage market as the secretary "deems necessary."

The measure sets no limit on how long Treasury could hold the assets, which must have been issued before Sept. 17. But the goal would be to sell them after housing prices recover and to earn back much of the money.

To cover the cost of the program, Treasury would have to borrow $700 billion, a sum Sen. Charles E. Schumer (D-N.Y.), the chairman of the Joint Economic Committee, yesterday called "breathtaking." Since 2003, Congress has appropriated just more than $600 billion for the Iraq war. The rescue package could exceed that in a matter of months, but the government could potentially recoup its investment if it is able to resell troubled assets at a profit.

To accommodate the new debt, the proposal seeks to increase the legal debt limit to $11.3 trillion. The limit was last raised in July -- to $10.6 trillion -- when Congress gave Treasury Secretary Henry M. Paulson Jr. authority to salvage struggling mortgage finance giants Fannie Mae and Freddie Mac. The nation's debt currently stands at $9.6 trillion.

It is unclear how the new spending would affect the annual deficit, which is already at near-record levels. Taken together with Treasury's promise to spend up to $200 billion to keep Fannie Mae and Freddie Mac solvent, budget experts said the broader rescue plan could easily leave the next president facing a budget hole that approaches 6 percent of the overall economy, a tide of red ink not seen since the Reagan administration.

At a meeting Thursday in the Capitol, administration officials told lawmakers the bailout would cost about $500 billion, but they did not have a good estimate at the time, according to sources familiar with the matter. Final calculations were completed just before the proposal went to Congress.

A number of other provisions were also in play, including whether the bailout should include securities backed by loans other than mortgages. In the end, Treasury decided to focus only on residential and commercial mortgages.

Commercial mortgages have become a concern for regulators as the delinquency rate hit 8.1 percent at the end of June, the highest rate for any category of bank loans, according to the Federal Deposit Insurance Corp. The rate more than tripled from 2.4 percent at the end of June 2007, and the trend already has caused some bank failures.

Treasury also considered permitting foreign firms active in the United States to participate in the program, but decided instead to push other nations to rescue their own companies.

Yesterday, British Prime Minister Gordon Brown said his government would do "whatever it takes" to "sort out the financial system." Brown said he realized earlier this week, when he was notified that Britain's biggest lender, HBOS, was facing collapse, that "we are in a different world."

An official at the Bank of England who spoke on condition of anonymity said the bank has been in constant contact with its U.S. counterparts to try to win a "global response to a global problem." The European Central Bank declined comment.

On Capitol Hill, Democratic and Republican leaders gave the proposal somber reviews and promised to act quickly. Paulson has asked that the plan be approved before Congress adjourns Friday in advance of the November elections. Frank said lawmakers could meet that goal, even with the addition of several controversial provisions favored by House Democrats.

Frank said the most nettlesome is likely to be their demand that bankruptcy judges be authorized to modify mortgages on primary residences, as they now can for second homes. The banking industry fiercely opposes the idea, saying it would drive up mortgage interest rates, and a similar proposal failed in the Senate earlier this year.

House Speaker Nancy Pelosi (D-Calif.) also plans to renew her campaign for a second stimulus package. Democrats have called for spending about $50 billion on highway projects, unemployment benefits and other social programs to create jobs and stimulate consumer spending.

Those provisions are likely to anger conservatives. But a Democratic aide said they would be needed to rally votes for a hugely expensive bailout plan that might be opposed by fiscal hawks in their own party as well as some Republicans.

Republican leaders yesterday warned against loading up the measure with Democratic priorities. "Now is not the time for partisan plans or pet projects," Senate Minority Leader Mitch McConnell (R-Ky.) said in a written statement.

But Frank and Schumer said Paulson has been open to negotiation.

"The secretary is feeling even more pressure" from economic conditions, Frank said, adding that he has told both Paulson and Federal Reserve Chairman Ben S. Bernanke to continue to exercise their emergency powers to stabilize the economy while the legislation is pending.

Paulson worked the phones all day Saturday, urging lawmakers to act fast. After briefing representatives from both parties and both chambers, Treasury officials said they remain confident the bill will win quick approval.

Staff writers Dan Eggen and Binyamin Appelbaum contributed from Washington, Mary Jordan from London and Craig Whitlock from Berlin.

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