



March 2009

[www.ssd.com](http://www.ssd.com)

## Treasury Unveils Master Plan for US Financial Regulatory Reform

US Treasury Secretary Timothy Geithner's much-awaited testimony before the House Financial Services Committee on Thursday, March 26, 2009 confirmed that the Obama Administration's plan for reforming the prudential regulation of the US financial services industry will be comprehensive.

Promising "not modest repairs at the margin, but new rules of the game," Secretary Geithner identified four broad areas of a "comprehensive framework of reform." After reviewing what he believed to be the root causes of the current financial crisis in the United States, he indicated that the following areas would be addressed with rules that are "simpler and more effectively enforced" than existing regulations:

- Systemic risk
- Consumer and investor protection
- Gaps in the regulatory structure
- International cooperation

Acknowledging the plan's importance and its role at the center of the agenda of the upcoming G-20 Heads of State Summit in London on April 2, most of Mr. Geithner's remarks focused on the Administration's goal to address and reduce systemic risk in the US financial system in six ways:

1. **Single Entity:** The Systemic Risk Regulator (widely assumed to be the Federal Reserve, although Secretary Geithner, Fed Chair Ben Bernanke or President Obama have not confirmed that belief) would designate its regulated entities, presumably ending the choice financial

Founded in 1890, Squire, Sanders & Dempsey L.L.P. has lawyers in 32 offices and 15 countries around the world. With one of the strongest integrated global platforms and our longstanding one-firm philosophy, Squire Sanders provides seamless [legal counsel worldwide](#).

### Squire Sanders Financial Crisis Response Team

Visit our website page for up-to-the-minute information on events as they develop.

Please contact your principal Squire Sanders lawyer or a member of our [Financial Crisis Response Team](#).

Squire Sanders publishes on a number of other topics. To see a list of options and to sign up for a mailing, visit our [subscription page](#).

[Unsubscribe](#)

Cincinnati · Cleveland · Columbus · Houston · Los Angeles · Miami · New York · Palo Alto · Phoenix · San Francisco · Tallahassee · Tampa · Tysons Corner · Washington DC · West Palm Beach | Bogotá+ · Buenos Aires+ · Caracas · La Paz+ · Lima+ · Panamá+ · Rio de Janeiro · Santiago+ · Santo Domingo · São Paulo | Bratislava · Brussels · Bucharest+ · Budapest · Dublin+ · Frankfurt · Kyiv · London · Moscow · Prague · Warsaw | Beijing · Hong Kong · Shanghai · Tokyo | +Independent network firm

conglomerates have had since 1956 with the enactment of the Bank Holding Company Act to opt for or avoid bank holding company status. Nonbank payment system participants would be included if the regulator considers them to be sufficiently systemic. Legislation would specify the characteristics of systemic risk firms, specify the nature of their oversight and assign responsibility for specific supervision and regulation to existing or, perhaps, new regulatory agencies.

2. **Heightened Capital and Liquidity**

**Requirements:** Systemic risk firms would face higher capital, reserve and liquidity requirements, which would be more countercyclical than existing pro-cyclical ones and would not have the distorting effect of unbridled mark-to-market accounting. These more robust requirements would presumably entail less profitability than those applicable to the entities' nonsystemic risk competitors. This profitability differential might represent a market-driven strategy to reduce the number of "too big to fail" institutions by self-selected attrition. New regulation of the identity of counterparties and enhanced risk management rules would also be part of this re-regulation effort.

3. **Hedge Funds, Private Equity and Venture**

**Capital:** Reaffirming its difference with the viewpoints of European G-20 nations and with those of many US parties, the Administration's plan would not subject private investment funds to bank or insurance company types of regulation or even require the funds to register with the Securities and Exchange Commission (SEC). Rather, investment advisers to funds having assets under management that exceed a yet-to-be-established minimum size threshold would be required to register with the SEC under the existing Investment Advisers Act, and the confidential reporting of such advisers to the SEC would be shared on a confidential basis with the Systemic Risk Regulator. These reports would focus on the size and leverage of the particular funds and on the nature of the investors. Some commentators dismissed the distinction between SEC registration of a fund's investment adviser and SEC registration of a fund, interpreting the Treasury plan as requiring SEC registration of the funds themselves.

4. **Over-the-Counter (OTC) Derivatives:** Mr.

Geithner promised comprehensive new regulation of markets for, and the products constituting, credit default swaps and OTC derivatives. Standard contracts would be required and would be traded through designed and regulated "central counterparties." To the extent permitted, nonstandard contracts would be reported to trade repositories and subject to robust documentation, confirmation, netting, collateral, margin and close-out practices. Aggregate data would be made public, while individual firm trade and counterparty information would be made available to financial

- regulators on a confidential basis.
5. **Money Market Funds:** Acknowledging that money market funds have long been regulated by the SEC, Mr. Geithner promised a strengthened regulatory system for money funds to make the industry less susceptible to the types of runs that resulted from last fall's "breaking of the buck" by a major money market fund.
  6. **Nonbank Resolution Entity:** Mr. Geithner's plan includes a resolution authority for nonbanks modeled after the Federal Deposit Insurance Corporation (FDIC) with the flexibility to nurse nonbank financial institutions back to health via loans and investments by way of a conservatorship or to liquidate or sell them via a receivership. He emphasized that monies of the FDIC's Bank Insurance Fund would not be used for this purpose and outlined an elaborate system of approvals involving the Federal Reserve, Treasury, FDIC and White House that would be needed before launching a resolution of a systemically significant institution.

His remarks did not resolve whether the FDIC itself would be assigned to play this role (as FDIC Chair Sheila Bair and Mr. Bernanke seem to favor) or if a new agency similar to the FDIC would be created. House Republicans and others have questioned the constitutionality of a nonjudicial administrative agency being empowered to "resolve" a private non-insured depository business corporation.

With respect to the timing of congressional action, House Financial Services Committee Chair Barney Frank stated at the hearing that he would like to enact the systemic risk provisions of the plan within a few weeks, with the balance of the plan being passed by the end of this summer. Many observers believe that this timeframe is overly optimistic given anticipated industry opposition to many of the reform details and inevitable turf battles among regulatory agencies and among those agencies' supporters on various congressional committees and subcommittees.

Squire Sanders will continue to monitor the global reform process and distribute alerts that cover developments as well as the results of the April 2, 2009 G-20 Summit in London and the introduction of substantive legislative proposals before the US Congress.

---

The contents of this update are not intended to serve as legal advice related to individual situations or as legal opinions concerning such situations. Counsel should be consulted for legal planning and advice.

©Squire, Sanders & Dempsey L.L.P.  
All Rights Reserved  
2009

This email was sent by: Squire, Sanders & Dempsey L.L.P.  
One Maritime Plaza, Suite 300, San Francisco, CA 94111 USA

We respect your right to privacy – [view our policy](#)