

Viewpoint

One of a series of opinion columns by bankruptcy professionals

Fear And Regulation: Do They Go Hand-In-Hand?

By Scott Y. Stuart

It is safe to say that during the last year the U.S. economy has moved from unprecedented euphoria to unparalleled fear. The reasons for the same, including the seizure of the credit markets and such will be long debated after this era is past, as will the use of taxpayer money to theoreticly quell a total economic meltdown. The question posed today, however, is what is guiding the next steps on the road to recovery? Is it prudent economic reasoning or reactionary policy making to dispel fear?

This week, in a Washington Post op-ed titled "A New Financial Foundation," Treasury Secretary Timothy Geithner and Lawrence Summers, the director of the National Economic Council, unveiled the Obama administration's "foundation for a stronger and safer system." The plan, designed to highlight areas that need to be targeted and safeguarded in our economy, seems designed to hedge against the kind of systemic failures that may (or may not) be responsible for the current failings in almost all sectors of the U.S. economy. It will be regulation like never seen before. Coming out of the unregulated wild ride of almost a decade however, this may be too much government, too soon after the economic collapse.

The administration's plan, as a basic premise, indicates that the unregulated markets are now considered a negative in our economy. Thus, the pendulum is about to swing in the opposite direction. How far it goes however will be a test of balance between a free market economy and one regulated into the outer boundaries of a democratic society.

The plan to be unveiled highlights five "key problems" within the current regulatory regime that needs to be evaluated and changed. A review of the same, however, raises as many questions as it does to provide regulatory guidance aimed at long-term stability.

While the administration believes the best way to safeguard against system-wide financial stability is raising capital and liquidity requirements for all institutions, will that alone support credit confidence? While broader supervision of the financial system has merit, raising the bar on capital and liquidity requirements could have the unintended affect of further stressing the mid- and small-business sectors. If raising capital and liquidity requirements is the goal, risk aversion will be the result. Thus,

even good business models may still be bad credit risks in an environment where risk is being deterred as never before.

In response to the growth of a long stretch of unregulated lending, the administration seems poised to not only regulate the non-traditional lending sector, but to require those outside of the traditional banking sector to act more like traditional banks. It is not just reporting requirements that will be enhanced, but the possible requirement that an originator, sponsor or broker of a securitization have a financial interest in performance. While attractive in theory, again this poses significant challenges to a secondary market designed for a certain level of risk taking and assumption. How performance is measured may be the key to determine reasonableness of the level of regulation sought. Again, balance is important and over-regulation stands to be as damaging as no regulation at all.

Next, the administration's plan will attempt to create protectionist policy regarding what it calls "predatory lending and unfair practices." There is no doubt that this was a large problem which in the end caused the collapse of the subprime market, and arguably was the defining event of the more broad based economic collapse. The need for some form of regulation to guard against predatory lending practices seems reasonable. The issue here, however, is how regulation will address unfair practices, particularly when it comes to the credit card and annuity sectors. The face of these sectors, long regulated but not overly scrutinized, may now struggle to find its center, redefining under a watchful governmental eye, how credit is extended, paid and pursued. This is an unknown that could redefine an entire industry sector.

One of the most striking proposals that will be explored is how to address the failures of financial holding companies that threaten the stability of the entire financial system. It will be interesting to see how the threat is defined as well as how much authority regarding takeover or control of an institution the government will give itself. While Geithner and Summers indicate that this remedy is anticipated to be used in the most extraordinary circumstances, this level of regulatory authority could be perceived as limitless. In effect, a government panic button may be created, resulting in unchecked governmental power under the guise of protecting the economy from financial instability.

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The last broad-based issue that the administration is intent on addressing is global regulation and supervision, presumably tailored after regulation created at home. The theory here is interesting, but difficult to implement. While standards to avert a global financial crisis are important, U.S. interests are not always aligned with those of the European Union or China, for example. Much resistance will likely occur on this front, particularly in light of recent grumblings by China and others who have begun to question the long-term benefit of staying tied to the U.S. dollar.

The Obama administration, in its attempt to manage the current financial crisis and to create a more stable future, faces tough challenges in uncharted waters. It's no surprise that a greater level of regulation in virtually all sectors of the banking and lending communities is on

the horizon. The real challenge, however, will be to regulate just enough to redefine the landscape while at the same time leaving an open door to a more liberal free-market system. More than anything else, this highlights the importance of sound regulatory policy that is not driven by fear.

Opinions expressed are those of the author,
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Firm Retention Summary

White Energy Inc.

This is a summary of a request from White Energy Inc. to hire Ice Miller LLP as counsel, filed May 26 with the U.S. Bankruptcy Court in Wilmington, Del.

COMPANY: White Energy Inc.

FIRM TO BE HIRED: Ice Miller LLP

PRINCIPAL ASSIGNED TO THE CASE: Henry A. Efroymsen

DUTIES: The firm will provide the following services:

- providing legal advice to the debtors with respect to their rights, powers and duties as debtors in possession in the continued operation of their business and management of their properties;
- taking all necessary action to protect and preserve the debtors' estates, including the prosecution of actions on the debtors' behalf, the defense of any actions commenced against the debtors, the negotiation of disputes in which the debtors are involved, and the preparation of objections to claims filed against the debtors' estate;
- preparing and pursuing confirmation of the debtors' plan(s), approval of the debtors' plan(s) and approval of the debtors' disclosure statement(s);

- preparing necessary applications, motions, answers, orders, reports and other legal papers on behalf of the debtors;
- appearing in court and to protect the interests of the debtors before the court; and
- performing all other legal services for the debtors which may be necessary and proper in this proceeding.

HOURLY COMPENSATION: Members of the firm will be compensated at the following hourly rates:

Partners	\$325-\$525
Of counsel	\$225-\$440
Associates	\$205-\$350
Paralegals	\$155-\$235
Henry A. Efroymsen	\$485
Michelle J. Fisk	\$350

BONUS POTENTIAL: Not applicable.

CASE BACKGROUND: White Energy, an ethanol company, filed for Chapter 11 bankruptcy protection on May 7.

HEARING DATE: A hearing on the matter has been scheduled for June 11.