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Geithner Wants New Rules to Check Risks

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WASHINGTON -- Treasury Secretary Timothy Geithner will call Thursday for changes in how the government oversees risk-taking in financial markets, pushing for tougher rules on how big companies manage their finances as well as tighter controls on some hedge funds and money-market mutual funds.

The move represents an early salvo in what will likely be a long debate about how to overhaul the rules governing markets, an effort officials say is designed to help restore confidence in the U.S. financial system. It comes just days before Mr. Geithner and President Barack Obama travel to London to meet with other global leaders to discuss the crisis.

The Treasury has been rolling out its proposals piecemeal. It announced Wednesday a central plank of the U.S. effort: a call to give powers to the Treasury and Federal Deposit Insurance Corp. to seize any company whose collapse could put the broader economy at risk.

Thursday, at a Congressional hearing, Mr. Geithner is expected to focus on changes that he believes are necessary to contain "systemic" risks to the economy. The Obama administration is working on other changes, too, including beefed-up consumer and investor protections.

Mr. Geithner is expected to call for a strict and consistent set of regulations for large firms, as well as more power for the government to monitor emerging risks to the economy. The new rules will likely require financial institutions to hold more capital as a buffer against losses and will bolster risk-management standards. All told, the proposals would mean significant expansions of power for the Treasury, Federal Reserve and other regulators.

It isn't clear which companies would be brought under this umbrella. Administration officials believe they could include banks' parent companies, insurance conglomerates and certain hedge funds, among others. They said it would depend on a company's size, leverage, reliance on short-term funding and role in the financial system.

One area where the U.S. is departing from its European allies is the Obama administration's approach to hedge funds, private-equity firms and venture-capital funds. Mr. Geithner is expected to ask Congress to require all of these firms over a certain size to register with the Securities and Exchange Commission and disclose certain information so government officials can determine whether their size or complexity puts the broader economy at risk.

This provision stops short of stricter proposals some European leaders have floated, calling for hedge funds to be regulated like banks.

Administration officials want Congress to give the SEC more power over money-market mutual funds so that the government can limit the risk profiles of these companies. Fears about the stability of these funds led investors to flee these products during the height of the financial crisis last fall.

Mr. Geithner is also expected to call for changes in rules governing how banks conserve cash to cover losses, with the goal of allowing them to set aside more when times are good. He also will call for a review of "fair value" accounting rules that require banks to take losses when the price of their assets falls. Some critics argue such rules punish firms when they need help the most—during rough times.

Already in process is an effort to give the government the ability to wind down a financial company whose failure could shock the broader economy, such as investment bank Lehman Brothers Holdings Inc. or insurer American International Group Inc. Mr. Obama, echoing calls from the Bush administration, has argued many of the repeated bailouts of recent months could have been avoided had the government had those powers.

"Because we have learned from the current crisis that destabilizing dangers can come from financial institutions besides banks, our plan will give the government the tools to limit the risk-taking at firms that could set off cascading damage," Mr. Geithner told the Council on Foreign Relations on Wednesday, the same day the Treasury laid out how such a process might work.

Government officials believe the new authority might give policy makers a powerful club to demand strategic or management changes at companies.

Policy makers have been split over which agency to entrust with the power to take over large, failing financial companies. The Treasury has the financial clout, but the FDIC has more experience handling failed companies. The FDIC, an independent agency, is also preferable to some, who worry the Treasury may be seen as too political.

Mr. Geithner's proposal would allow the Treasury and FDIC, in consultation with the Fed, to jointly determine if a company needed to be seized. It would then entrust the running of the company to the FDIC, allowing the agency to borrow money from the Treasury. House Financial Services Committee Chairman Barney Frank (D., Mass.) is expected to introduce legislation soon that would give the government the power to seize a failing financial institution that isn't a bank. Senate Banking Committee Chairman Christopher Dodd (D., Conn.) said he "welcomed the proposal."

The Treasury's proposal would let the government take over the parent companies of banks, thrifts, and broker dealers, as well as major hedge funds, insurance companies and futures commission merchants.

The proposal would allow the FDIC to sell the company's assets and renegotiate or reject existing contracts. This could give the government leverage to ban bonuses at struggling firms, but it could also raise questions among counterparties as to whether existing contracts might survive government seizure.

The FDIC would also be able to replace directors and senior executives and "none of these actions would be subject to the approval of the institution's creditors or other stakeholders," the Treasury said.

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