



Federal Financial Analytics, Inc.

Post-Rescue Regulatory Rewrite Reviewed

“Treasury and the FDIC now hold shares in privately-owned companies and, perhaps, more warrants are in the offing. This is an awesome paradigm shift that presages a complete overhaul in financial regulation as we know it. In addition, there is a daunting array of statutory and regulatory changes to come in areas like capital requirements, the powers of bank holding companies now that everyone who’s anyone is one, the future of OTC derivatives and “shadow” financial institutions, deposit insurance and the regulatory structure that will govern all this.”

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NEW YORK, NEW YORK – Even as Congress advances the economic-rescue package, massive changes to the regulation of the U.S. financial-services industry are already under way. In remarks today before a conference of general counsel from the nation’s largest banks, the managing partner of Federal Financial Analytics, Karen Shaw Petrou, identified those already clear in the midst of the market maelstrom.

“If you read through a “blue-ribbon” industry report of mid-2005, you’ll see a remarkable outline of everything that’s gone wrong since then and a nice set of recommendations on how to fix them,” Petrou noted. However, nothing was done thereafter and, Petrou said, “The industry and its regulators have little, if any, credibility. There’s nothing like a \$700 billion

rescue plan, hundreds of billions of Fed funds and a series of systemic-risk failures among the GSEs and large banks to concentrate the mind,” she continued.

Specifically, Petrou concluded that tough new capital standards will not only govern regulated institutions, but also indirectly govern hedge funds, private-equity firms and other “shadow” banks. While this will be costly at first, the changes will also create a significant opportunity for regulated, well-capitalized lenders and insurers – an important silver lining in the current market storm clouds.

Petrou also focused on the impact of the Treasury’s protection for money-market mutual funds (MMFs) and the pending expansion of federal deposit insurance. She noted that these new full-faith-and-credit protections will come at the cost of significant new regulation. These rules will cover not just the capital and other prudential standards reference above, but also new social-policy requirements similar to the Community Reinvestment Act now governing banks.

Finally, Petrou addressed the future of the bank holding company “now that anyone who’s anyone is one.” She noted the strong prospects for a regulatory requirement that treats bank holding companies like utilities – trading all the billions in rescue support from the federal government provided now for a tough new supervisory framework that limits salaries, controls prices and redictates infrastructure improvements in areas like the derivatives market. Petrou noted that this isn’t necessarily what she would recommend, but rather how the next Congress and new President will, she said, start the debate.

The full text of the Petrou speech is attached.

Federal Financial Analytics, Inc. has for the past twenty years counseled large financial institutions and even their regulators on major legislative, regulatory and policy issues that pose strategic risk. It does not lobby on behalf of clients, but advises them on appropriate responses in light of identified challenges, working on an array of GSE, Basel II, and acquisition-value issues. The firm publishes numerous information and analytical services, including Financial Services Management and GSE Activity Report.

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