

# Legislative Highlights

## *Senate Bills Would Regulate Hedge/PE Funds, Create Consumer Financial Product Safety Commission*

The “regulation and transparency” fervor of the 111th Congress is evidenced by two recent Senate bills—each inspired in their own way by the current financial meltdown. The “Hedge Fund Transparency Act” (S. 344), introduced by Sens. Chuck Grassley (R-Iowa) and Carl Levin (D-Mich.), would compel hedge funds, as well as private equity and venture capital funds, to register with the Securities and Exchange Commission (SEC), requiring funds to disclose investors’ identities, adopt anti-money-laundering programs and require funds to report suspicious transactions. The bill, similar to one introduced but stalled in the last Congress, would remove the loophole previously used by hedge funds to escape the definition of an “investment company” under the Investment Company Act of 1940, and established in a 2006 opinion by the U.S. Court of Appeals for the Washington, D.C., Circuit. The Act would legislatively overrule the decision and provide the SEC with the authority needed to impose additional regulatory safeguards. The systemic and high risks associated with hedge funds have come into sharp focus because of the growth in the number and size of the funds, and the mix of assets invested by state pension plans,

university endowments and charities. The result is that hedge fund losses are now not confined to sophisticated, direct investors, but can ripple through the entire economic sector. Hearings are expected in the Senate Finance and Government Oversight committees.

The new era of more muscular regulation applies not only to the investor class, but also the consumer class: On March 10, Sens. Dick Durbin (D-Ill.) and Chuck Schumer (D-N.Y.) introduced the “Financial Services Product Safety Commission Act.” Modeled on a proposal by Harvard Law professor **Elizabeth Warren**, the bill would create a new federal commission, modeled after the Consumer Product Safety Commission (CPSC), which would be charged with a broad responsibility to establish guidelines for consumer disclosure, the review of new products for safety, modification of existing consumer financial products and collection and reporting of data to Congress and the public. The new agency could review mortgages, credit cards, car loans and other consumer financial products for the purpose of identifying and eliminating hidden terms and conditions that make them more dangerous to the financial health of the consuming public.

The commission could ban certain credit products or practices, promote uniform disclosures that make it easier for consumers to comparison-shop for consumer financial products, and encourage more consumer-friendly terms and conditions. Prof. Warren has long argued that a flaw in the existing free market of financial products is that these products are treated as “contracts” rather than “products.” These contracts are between parties of unequal bargaining power and permit the lenders to unilaterally change the terms to make the credit offering more dangerous to the financial health of the consumer. The CPSC, established in the early 1970s, has helped keep dangerous products out of the marketplace through standards and regulations, and the new agency would be similarly empowered to ensure that American financial products are equally safe when used as intended by consumers. Hearings are expected in the Senate Banking Committee.

Both bills will face opposition in the Senate. Whether the current crisis environment is enough to sustain the momentum for a pro-regulatory response remains to be seen. ■