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Symposium Foreword

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REGULATION AND RECESSION: CAUSES, EFFECTS, AND SOLUTIONS FOR FINANCIAL CRISES

SYMPOSIUM FOREWORD

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The barbarians of the economic apocalypse are no longer battering down our gates, but we can still see their camp fires from the top of our crumbling walls. In fact, it was only a few months ago that many commentators had the dreaded d-word, depression, constantly on their lips. Many of them are still fearful, and rightfully so, pointing to persistently high unemployment numbers, stagnant or even shrinking wages, and a volatile, seemingly "irrational" stock market as evidence that we should remain ever more worried about our future prospects for recovery. Were these problems ours alone, the task might not seem so daunting, but these problems appear to afflict every country in the world in one way or another. Thus, while we may have cracked open our defenses for a few timid forays outside, it seems that it will be a long while yet before we have the confidence and resolve to recapture the vigor, flexibility, and innovation that helped drive our economy for the better part of our recent history, helping to lift many out of poverty as well as to bring about countless radical changes in our society, both for good and bad.

Against this larger backdrop, our country has been consumed by a familiar debate centering on government's proper role in relation to the broader economy (or even if, indeed, there is a proper role for government to play). It goes without saying that the debate is a contentious one. While I will not repeat the all too common refrain that our country has suddenly become more polarized, I do believe that it has become more polemical. Various commentators point to different sources for this phenomenon. Some blame the internet, discussing the evils engendered by its unlimited, largely unfiltered content and the virtual anonymity that is bestowed upon those who wish to be heard on blogs and news aggregating websites. Others claim that it is talk radio, the mainstream media, or the fear and uncertainty engendered by a rapidly globalized culture that is shoehorning people into increasingly isolated ideological communities according to their predispositions. Whatever the reason for this new, pugnacious discourse, its effects are being felt in public life; arguments are bitter, common ground is scarce, and selfrighteous certainty, something that should be largely unwelcome in a democratic society, runs rampant.

So it is that our economic debate, spurred on by our economic crisis, has come upon us in this era of absolutes. In keeping with our times, then, one's opinions regarding the so-called "dismal science" appear to be becoming more and more central to our interpretation of events and prescriptions for change. In fact, economic theory is quickly turning into a proverbial third rail in American social life, something about which, like politics and religion, everyone has a strongly held opinion that, for the sake of a peaceful dinner table, they mostly keep to themselves. More troubling still, it appears that economics, like any important concept in contemporary life, has shown signs of morphing into an object of modern idolatry, with some worshiping at the altar of the free market and others at the shrine of government regulation. Combine this development with our penchant for absolutes and it now seems that where a person stands with regard to any number of issues relating to our economic well-being, be it price controls, tort reform, bailouts, or taxes, has become in the eyes of many as important an indicator of character and trustworthiness as a person's upbringing, education, and morals. This makes it difficult, in the least, to have an honest and open conversation about our current predicament.

Much ink has been spilt over the past few months by commentators, scholars, and policy wonks disputing the virtues of everything from bailouts to bankers, socialism to deficits, but very few have put forth the sort of reasonable and measured dialogue that is called for in such trying times. Rather than come to the table with solutions that, while perhaps not wholeheartedly endorsed by all sides, are at least acceptable to a broad majority, many have come armed only with dogma and certainty, ready for a "battle-to-the-death" of ideologies. Solving our problems, it seems, is of only secondary concern.

It is in this context, then, that this symposium came into being. It is my hope that these five articles will stand as a small albeit *rational* contribution to this important discussion. Focusing on developments in our own nation, this collection presents succinct accounts of where we've come from as well as cogent suggestions for where we should go from here. And, while it is filled with strong opinions, this symposium does not add to the discourse of one side or the other but instead thoughtfully and equitably contributes to the ongoing conversation over government's duties and failures in the economic realm. It will hopefully give readers pause to think and reexamine their own beliefs as well as provide practical measures that may help us as we move farther away from the recent crisis.

Before delving into our subject, however, I would like to briefly sketch the problem that appears to be lurking in the background of our current debate, one that few are willing to speak of and even fewer are willing to admit exists. The problem centers around the concept (and, regrettably, the buzzword) of "sustainability." This symposium's subject, government regulation, is intimately connected to this larger concept. After all, anything that a government does or refrains from doing in relation to the economy should be done with an eye towards its perpetual health; i.e. it should be sustainable. I grant that this concept presents us with, if nothing else, a rather nebulous standard or goal with which to measure our achievements. In recent years, sustainability has largely been associated with environmental concerns[1] and, at least in that context, it can plausibly be argued that the word has been co-opted to the point of meaninglessness since every entity now claims to be sustainable in one way or another with little regard to the reality of its situation. But despite the fog that surrounds this concept, I would still argue that coming to grips with a sustainable economy is vitally important for our future success in the global marketplace.

Here, then, in the wake of this most recent crisis, we are presented with an opportunity to have a nuanced discussion about sustainability and how its lessons might influence our economic future. In beginning such a discussion, we need only ask one question: can we continue going down the path that we are on? I readily admit that the question is a simple one, some would even say it is too banal for serious contemplation, but I believe that its subtext is quite profound when considered in light of the current state of the world economy. For instance, it can be read very narrowly to fit a specific situation. In this way we may inquire whether, for the sake of sustainable lending, the banking industry should be forced to give up the extravagant practices of securitization that have played an outsized role in creating the current credit crunch. Similarly, the question could be used to probe accounting rules, predatory lending practices, executive compensation, or any of the other current hot topics of debate taking place in economic circles.

Perhaps more importantly, however, the question should be considered from a much broader perspective. Some might phrase the question in this manner: is it feasible for everyone in the world to be striving towards a house in the suburbs with a two-car garage? I don't mean to ask this in a disparaging way to those who do, indeed, desire such things. Nor do I naively believe that every person on the planet, all six billion of them, aspire to this same dream. All the same, it seems certain that most people aspire to a "better" life, a change which often requires an advance in one's material circumstances. The true kernel of the question, then, is difficult to answer. It boils down to this: with the rapid transformation of many former third-world countries that are now aiming for first world affluence, are the practices, beliefs, and regulations that have prevailed in wealthier countries over the past few decades up to the task of ensuring stability in the world's markets as more and more participants exploit fewer and fewer resources?

This question is not meant to rehash disputes that are better left to abler minds, if not relegated entirely to the history books. I have no desire to speak of the division of labor or the viability of private property rights, at least not in the abstract. Such things appear to have been decided, no doubt many of them for the better. The possibility remains, though, that there is a fixed limit to the amount of wealth that can be created by human endeavors.[2] After all, what does one do after the last arable piece of land is farmed? Even so-called renewable resources captured by wind turbines or solar panels

1. Though it cannot be doubted that the economy and the environment are tied together at their most fundamental level. *See* Jared Diamond, *Collapse* (Viking Adult 2004).

2. As Locke teaches, we can only have property (and, therefore, wealth) by mixing our labor with natural resources. John Locke, *An Essay Concerning the True Original, Extent and End of Civil Government*, in *Social Contract* 3, 24 (Oxford U. Press 1952) ("Whatsoever, then, he removes out of the state that nature hath provided and left it in, he hath mixed his labour with it, and joined to it something that is his own, and thereby makes it his property.").

do not promise limitless growth once we lack the space or materials required to build such complex devices. Although many will rightly denounce such an observation as dangerously Malthusian in bent (and Malthus has been, like Marx, wrong in his predictions up until now, [3] having discounted the ability of society to innovate and solve problems that once stood as roadblocks to our modern lifestyles), the principle itself should not be completely discounted.

As a quick illustration of the limits of growth, I would point again to the fad of securitization and derivatives that recently swept Wall Street. This practice, while not the only cause of the financial contraction, certainly played a central role in it. The premise was simple: make money by putting out a product, just as any other business would do. The product, however, quickly became a problem. Derivatives are, in effect, a hodgepodge of different interests gleaned from a large pool of loans. As the theory goes, so small an interest in so many loans offers security for those who want to buy these products. If one loan goes bad, no problem, the lost income is nearly negligible and the derivative will still retain the bulk of its value. Before the crisis, faith in such products grew to the extent that even derivatives formed out of poor quality loans were prized commodities. The market for derivatives expanded which, in turn, fed demand back into the mortgage industry causing more lenders to make ever riskier loans. When the music stopped, what had at one time appeared to be sound investments turned out to be worthless pieces of paper as countless mortgages went into default. The engine that had been driving investors' faith in derivatives had been the assumption that an endless number of people could continue paying an endless number of mortgages. When this assumption turned out to be false, the wealth that these instruments had "created" quite literally vanished as if it had never existed. In a way, though, it never did really exist; the value of each derivative, after all, did not rest on reality but rather on perception, thus necessitating an inevitable "correction" that brought everyone back down to earth.

Coming back to the question that prompted this illustration, then, we must ask whether the current financial and economic assumptions that underlie our markets rest on solid ground. Many of these assumptions may turn out to be valid, others may need adjusting; our examination may cause us to reconsider our deeply held economic beliefs in the name of pragmatism and common sense. To be sure, such reassessments have historically been painful. It would seem preferable, however, to engage with these difficult questions now than to have them forced upon us when the next crisis comes. After all, as the world's economies continue to be woven together through globalization, the "next crisis" will always have the possibility of being bigger and more devastating than those that have come before it.

It should not be assumed that such an important conversation will necessarily lead to a world intent on ascetism where the adoption of stringent austerity measures are considered necessary for the preservation of society. Maybe things do not need to change too much, maybe not at all.[4] Whatever the case, this brief foreword is not intended to

3. *See* Thomas Malthus, *An Essay on the Principles of Population* (Dover 2007); Karl Marx, *The Communist Manifesto* (Penguin 1967).

4. Although, despite what Dr. Pangloss would have you believe, this is almost certainly not the most perfect of all worlds. *See* Voltaire, *Candide* 4 (Pocket Books 2005) (" 'It is demonstrable,' he said, 'that things cannot be otherwise than as they are, for all being created for an end, all is necessarily for the best end.' ").

serve as a call for some bold new plan of action or a radical reshaping of our daily lives or our beliefs. But the fact remains that these questions should be asked and asked honestly, without regard to the current economic conditions, or better yet, expectations, that prevail around the world.

Despite what many would have us believe, as we stand now, things are by no means beyond repair. It goes against the greater weight of history to believe that we will forever be sliding listlessly towards economic ruin (or environmental, social, moral, or political ruin, take your pick). Such fatalism is perhaps related to the ideological rigor of our times and is a popular view to espouse, judging by what many commentators preach. It must be pointed out, though, that such talk has been with us for some time. Prominent thinkers have been certain of this slow march to oblivion at least since the poet Hesiod who lived in Greece around the 8th century B.C. [5] Hesiod's age of iron was certainly a violent and brutish one and he should be forgiven for thinking that such an inescapable fact presaged the coming downfall for the greater mass of humanity. It must be admitted, however, that humanity has endured for the greater part of the intervening three millennia. It has even prospered, at times.

Still, it should not be forgotten that even today millions of citizens who live in countries as diverse as Sierra Leon, Haiti, Afghanistan, and Cambodia would not find much fault with Hesiod's outlook. There are still a great many problems with which we as a global society must deal. And here I do not mean to conflate tragedies born of war, famine, or natural disaster with the tragedies of wealth that are the subject of this symposium, but I only wish to point out that problems exist and will persist until they are dealt with openly and honestly. Among these problems, determining government's proper role in the economy remains an important goal, one that may require people from across the ideological spectrum to abandon their theories in favor of more practical solutions so that *all* may prosper in the years to come.

That, then, is the global view of the problem; this symposium, however, deals primarily with the problem as it relates to our own country. This collection does not propose to solve any of the ideological arguments underlying the problem nor does it provide any easy explanations for the current crisis, its causes, or its effects. It is hoped, however, that this issue will go some small step towards furthering the economic debate in which our country is presently engaged by discussing the current crisis and the regulations (or deregulations) that may help to bring us back to prosperity. Underlying this whole discussion are the philosophical debates that I alluded to above, but here you will not find generalizations or ideological purity. Instead, the authors take practical steps towards solving real problems, putting forth suggestions that are meant to address our concerns about the economy, not reinforce our entrenched positions. The articles are arranged from those dealing with more generalized topics to ones with a more specific focus and they all have something very definite to say about where we are and where we should be.

5. Hesiod, *Works and Days* in *The Norton Book of Classical Literature* 191, 193–194 (Bernard Knox ed., Apostolos Athanassakis trans, W.W. Norton & Co. 1993) ("This is the race of iron. Neither day nor night/ will give them rest as they waste away with toil/ and pain . . . . [G]rief and pain/ will linger among men, whom harm will find defenseless.").

This symposium begins with a concise overview of the financial crisis written by Professor Daniel Morrissey. Professor Morrissey rightly criticizes the actions taken (or not taken) by the many players who had a role in the current crisis, not the least of whom were the government regulators who are charged with protecting our economy from such destructive instability. He also provides an overview of some of the reforms that have been suggested as a result of the crisis, analyzing them each in turn. Finally, pointing to a glut of inadequate regulations, Professor Morrissey suggests several reforms and initiatives that will strengthen our nation's defenses against such catastrophic economic fallouts in the future.

Professor M. Thomas Arnold continues in this vein, playfully and intelligently exploring the economic failures of both the private sector and its government regulators. Touching on a broad range of corporate shenanigans including off-shore accounting, insider-trading, stock option backdating, and ponzi schemes, Professor Arnold provides a primer on the recent history of corporate regulation, showing how each different scandal or crisis brought about new regulations that, while supposedly tailored to ensure the future stability of the marketplace, oftentimes only muddied the water with duplicative requirements that rarely if ever fully addressed their animating concerns. In order to break this cycle, Professor Arnold makes two common sense proposals: allow regulators to be liable for their misdeeds and create a system of bounties that will reward whistleblowers who expose corporate malfeasance. Both proposals are simple and direct, aimed at making our economic system more equitable and transparent. Moreover, unlike other laws that have been enacted after corporate scandals, these proposals may actually *prevent* a future crisis by making regulators more vigilant rather than providing them with yet more regulations that they are neither willing nor able to enforce.

Professor Gregory Crespi's article transitions us away from those articles that are more generally concerned with the economic system as a whole towards articles that have instead isolated a single, albeit significant issue for discussion. Here, Professor Crespi focuses on the housing market and, in particular, immigration reforms that may halt or even reverse the recent slide in real estate prices. Drawing on a proposal made by Richard Lefrak and Gary Schilling, Professor Crespi persuasively argues for the creation of a program that would provide green cards to foreign investors who desire to buy real property in the United States. At first blush, such a proposal might seem to be too controversial to succeed in the wake of recent events; all the same, it should be seriously considered. The housing market, according to common wisdom, was the epicenter of our most recent crisis, and we would do wise to entertain any measure that purports to solve our problems in that sector of our economy.

Professor Timothy Hurley continues with this theme of reform, turning his attention to the problems that attend retiree benefits in this country. This topic has taken on added importance in recent years as the baby boomer generation makes its way to retirement. Moreover, one cannot help but recall the headlines over the past year describing many retirees' shock as they helplessly watched their once impregnable 401k's lose a substantial percentage of their value due to market fluctuations. In response to these concerns, Professor Hurley turns his attention to Voluntary Employee Beneficiary Associations (VEBAs), a relatively new form of retiree benefit plan that is quickly becoming popular throughout the country. He diligently lays out and analyzes the regulatory structure of VEBAs and provides several suggestions about how they might be made more responsive to the realities that retirees currently face.

Finally, Professor Rafael Efrat rounds out this edition by providing a detailed study of women business owners in bankruptcy. While this topic may seem a bit tangential to a "regulatory" issue, it actually goes to the heart of it, providing practical information that can be utilized by those who are charged with drafting the policies that direct our economic life. To be sure, when an entrepreneur declares bankruptcy, no regulatory response will repair the economic damage that has been done. However, by examining how and why people go into bankruptcy, regulations may be more discerningly crafted to prevent such catastrophic events by correcting any problems that are identified in the data. Professor Efrat provides a wealth of information on an ever growing and critical segment of those who file for bankruptcy, women entrepreneurs. With this study future regulators should have a better grasp on the causes of bankruptcy as well as some new ideas on how to craft preventative cures.

In conclusion, this symposium does not hold the key to preventing future crises or the secret to striking the right balance between government intervention and private enterprise. Rather, it is intended to be a modest contribution to the discussion currently surrounding our economic lives. Whatever one's predisposition towards the topic, he or she should find the articles presented here to be accessible, insightful, and challenging. Moreover, while this symposium may not shatter the ideological chains that currently constrain our debates or serve as a definitive guidepost for sustainable economic growth, if readers approach it with an open mind, it may yet provide pragmatic solutions to real world problems. After all, in our times, what could be more subversive than that?