

Four Initiatives to Change Banks' Structures and Business Models

The use of public funds to recapitalise failing banks during the global financial crisis of 2007-2009 ignited a debate on the proper activities of banks. The initial perception, promoted in the U.S. by Paul Volcker, was that taxpayers had covered losses incurred by banks trading in abstruse financial instruments that had no public utility but which could generate huge profits for a few individuals during good times. Volcker therefore proposed that banks should not be allowed to trade for their own account ("proprietary trading") and instead be required to engage only in client-based business. The U.K.'s Independent Commission on Banking ("Vickers") took a broader approach to essentially the same issue and proposed separating into distinct legal entities client related business with evident social utility, and other banking activity. Legal entities conducting the socially useful activities would be required to hold significantly greater levels of capital, but would implicitly have access to state support in a crisis. Importantly, all legal entities could be part of a single group (i.e. under a single holding company).

The conceptual difference between the two approaches is that Volcker identifies a few specific activities which are deemed to have no place within the banking system (but could be appropriately conducted by say, hedge funds) whereas Vickers defines the banking services which an economy needs and ring-fences them within a highly-capitalised entity which can implicitly count on state support *in extremis*, but it does not proscribe other banking activities as long as they are conducted outside the ring-fence and do not expect state support.

The Liikanen Report, written for European Commissioner Barnier, is closer to Volcker in its philosophy in that it proposes to proscribe activities of perceived marginal social utility. More generally, Liikanen is concerned by the widening difference, in the years preceding the crisis, between economic growth and the growth in banks' balance sheets, and the implied shift in banks' business models.

The French *Projet de Loi*, presented to the French Assembly on 19 December, was driven largely by the need to fulfil commitments made by President Hollande during his election campaign. The proposal requires banks to place proprietary trading and certain other non-client facing activities in separate legal entities though they may remain part of the same banking group.

Liikanen, Vickers and the *Projet de Loi* also address issues other than the perimeters of banking – for example, Vickers addresses competition within the U.K. banking industry and the Project du Loi gives the Autorité de Contrôle Prudentiel new powers to resolve failing banks.

	LIIKANEN REPORT	VICKERS REPORT	(FRENCH) PROJET DE LOI	VOLCKER RULE
Date issued	October 2012	September 2011	December 2012	Initial proposals in 2009, and endorsed by President Obama in January 2010
Number of pages	133 pages	Final Report 358 pages. Government's proposed legislation is 17 pages (full document 84)	30 pages	Volcker's proposal to Obama was three pages. Section 619 of Dodd Frank (enacting it) is 11 pages. The regulators' joint Notice of Rule Making was 37 pages, with a further 493 pages of questions.
Next Steps	The consultation period ended in December and the Commission has published responses. There seems to be little appetite in Brussels to bring forward complex and controversial legislation at this late stage in the terms of the Commission and Parliament.	U.K. government has accepted key recommendations in the report, and will bring forward legislation in early 2013 to implement it.	French parliament will consider the proposal in early 2013 and will have to decide whether to move forward independently of any movement on Liikanen, some of whose recommendations overlap with the <i>Projet du Loi</i> .	Rulemaking expected to be complete early in 2013. Implementation delayed to mid 2014 though there are already requests for further delays.
Original documents	http://tinyurl.com/9pu4rcq	http://tinyurl.com/blclmly	http://tinyurl.com/b8ydm4o	http://tinyurl.com/3rgzl9p