Blinded by Volcker, Vickers, Liikanen, Glass-Steagall and Narrow Banking

Why these “solutions” will increase the risk of bailouts

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Too Big to Fail III: Structural Reform Proposals

Should We Break up the Banks?

Institute for Law and Finance

Frankfurt, Germany

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Davis Polk

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banking
Outline of Presentation

- Solutions in search of a problem
- Unintended consequences
  - Do nothing to cure disease
    - Ineffective proxies for regulating risks
    - Maginot lines that shadow banks simply drive around
    - Too rigid and brittle
  - Divert attention and resources from genuine cures
  - Hasten the patient's death

The Volcker Rule
Solution in search of a problem

“The Volcker Rule is a solution in search of a problem.”

– Jeb Hensarling,
Chairman, Financial Services Committee
U.S. House of Representatives

Hearing on Impact of Volcker Rule
January 15, 2014

- Last-minute addition to the Dodd-Frank Act
- No clearly articulated purpose
- Impossible to infer coherent purpose from text
- Inconsistent with philosophical underpinnings of rest of Dodd-Frank
- Yet now described by death-bed converts as central concept

The Volcker Rule
Unintended Consequences

- **IF**, as many argue, its **purposes** are to reduce risk of a covered bank's activities and end the TBTF problem, **THEN**:
  - No persuasive evidence it will actually achieve those purposes
  - Ample reason to believe it will:
    - Do nothing to cure the disease
    - Divert attention and resources away from genuine cures
    - Hasten the patient’s death

Vickers, Liikanen, Glass-Steagall, Narrow Banking
Unintended Consequences

- Same diagnosis applies to Vickers, Liikanen, Glass-Steagall and various Narrow Banking proposals
  - . . . . And any other proposal that attempts to reduce risks by separating "official" from shadow banking systems
- Diagnosis of all separation proposals:
  - Do nothing to cure the disease
  - Divert attention and resources away from genuine cures
  - Hasten the patient's death

Vickers, Liikanen, Glass-Steagall, Narrow Banking
Unintended Consequences (cont'd)

- Some separation proposals worse than others
  - Partial separation proposals (bad)
    - Vickers
    - Liikanen
    - Glass-Steagall as enacted in 1933
  - Total separation proposals (worst)
    - Volcker
    - Narrow Banking proposals
    - "Glass-Steagall" for the 21st century (really a narrow banking proposal)

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banking
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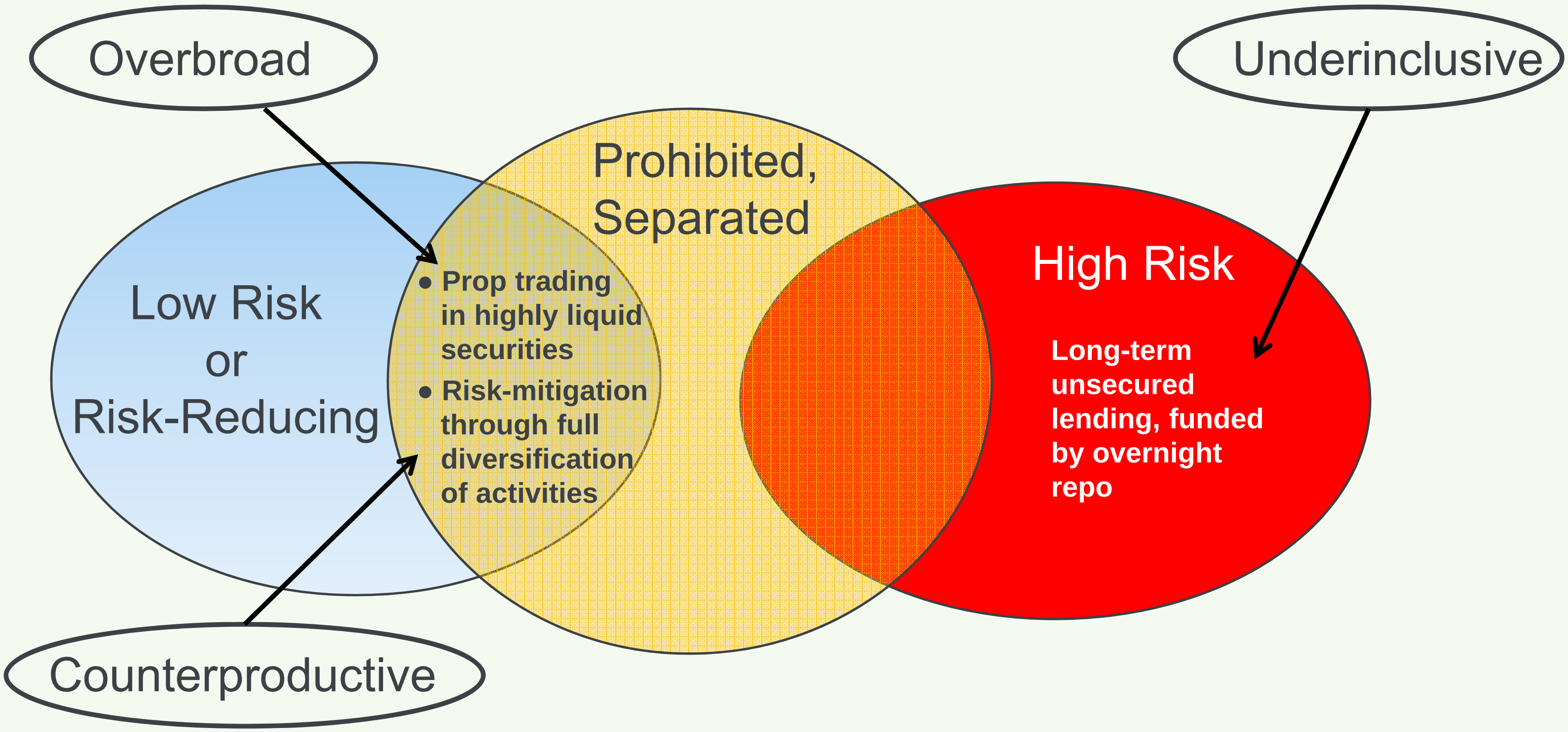
Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Do nothing to cure disease

- At least three reasons why separation proposals will do nothing to cure the disease:
  - Ineffective proxies for more direct ways of regulating risk
  - Like Maginot lines that shadow banks simply drive around
  - Too rigid and brittle
    - To respond to market reactions (political economy)
    - To adapt to ever-changing riskiness of official and shadow banking activities

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Ineffective proxies

- Ineffective proxies for more direct ways of regulating risk
  - Inevitably overbroad, underinclusive and counterproductive



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Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines

- Maginot lines that shadow banks simply drive around
  - Shadow banks will always find ways around exclusive money-making powers of official banks
    - Excess demand: More (almost insatiable) public demand for money and money market instruments than official banking sector has ever been able to safely and profitably supply
      - Official (legal tender) money: Coins, precious metals, bank notes, demand deposits
      - Unofficial money: Checks, NOW accounts, overnight repos, shares in money market mutual funds, prepaid payment cards, bitcoins, other forms of virtual money
    - With full public support

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Maginot Lines – History of banking in America

- History of banking in America illustrates futility of separation proposals
  - British Tunnage Act of 1694 and Bubble Act of 1720
    - Money-making monopolies: Granted monopolies to Bank of England and corporations like South Seas Company to issue paper money and money-like instruments
    - Shadow banks (pools of merchants or colonial governments – e.g., Rhode Island) in American colonies responded by issuing bills of credit
      - Not legal tender
      - But widely used as unofficial currency to make payments in private economy

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines – History of banking in America (cont'd)

- British Acts of 1741, 1751 and 1764
  - Severely restricted power of colonial shadow banking system to create paper money
  - Caused public uproar
  - Cited by Benjamin Franklin in 1767 as one of the reasons – along with Stamp Act and Quartering Act – for growing colonial hostility to British Parliament
  - Shadow banks in American colonies continued to circulate unofficial paper money used to make payments in private transactions

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines – History of banking in America (cont'd)

- American Constitution 1789
  - Granted Congress the power:
    - "To coin Money, regulate the value thereof, and of foreign Coin, and fix the Standard of Weights and Measures"
    - "To provide for the Punishment of counterfeiting the Securities and current Coin of the United States
  - Prohibited States from:
    - "coin[ing] Money; emit[ting] Bills of Credit; [or] mak[ing] any Thing but gold or silver Coin a Tender in Payment of Debts"
  - States responded by authorizing state-chartered banking corporations and unincorporated associations (shadow banks) to issue bills of credit and other forms of paper money and take demand deposits

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines – History of banking in America (cont'd)

- U.S. National Banking Act of 1864
  - Granted new national banks a monopoly to issue legal tender paper money
  - Companion statute in 1865 imposed a 10% tax on bank notes issued by state-chartered banks
  - State-chartered banking corporations and unincorporated associations (shadow banks) responded by encouraging the following close substitutes for legal tender paper money in making payments in the private economy:
    - Checks
    - Deposits that could be debited or credited by book-entry

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines – History of banking in America (cont'd)

- Glass-Steagall Act of 1933 and Various State Laws
  - Prohibited investment banks and other shadow banks (e.g., money market mutual funds) from engaging in the business of taking deposits
    - Still good law: Contained in § 21 of Glass-Steagall, which was not repealed by Gramm-Leach-Bliley Act of 1999
  - Investment banks responded by funding themselves with overnight repos and other forms of short-term credit
  - Money market funds responded by issuing debt securities that were redeemable on demand or within a matter of days

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Lines – History of banking in America (cont'd)

- Bank Holding Company Act of 1956
  - Originally prohibited any company that controls a bank engaged in taking demand deposits and making commercial loans from engaging in any activities other than banking or activities that are closely related to banking
  - Shadow banks responded by acquiring, or allowing their investment banking affiliates to operate as, "non-bank banks"
    - E.g., banks that did not fund themselves with demand deposits, but only with close substitutes, such as:
      - Deposits not legally withdrawable upon demand, but only upon 7 days prior notice, but which were in fact routinely withdrawn upon demand under ordinary economic conditions
      - Overnight repos

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Maginot Line

- Who were the shadow banks of yester-year?
  - Unofficial banks or colonial governments (e.g., Rhode Island) in colonial America
  - Commodities and other merchants
  - Wildcat banks (circa 1837 and after)
  - State-chartered banking corporations and private banks after the National Bank Act of 1863
  - Investment banks and money market mutual funds after the Glass-Steagall Act of 1933 and similar State deposit licensing laws
  - Securitization vehicles
  - Enron

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Maginot Line

- Who are the important shadow banks today or may be in the future?
  - Money market mutual funds
  - Walmart and similar superstores
  - Amazon.com, Facebook and Google
  - Online gambling companies
  - Online peer-to-peer lending clubs
  - Hedge funds
  - Bitcoin "miners" or prepaid card issuers
  - Telecom companies that sponsor mobile phone payment systems such as those widely used in Kenya and other parts of Africa
  - Other issuers of virtual currency

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banking

Outline of Presentation

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    - Ineffective proxies for regulating risks
    - Maginot lines that shadow banks simply drive around
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Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Too Rigid and Brittle

- Separation proposals are too rigid and brittle:
  - To respond to market reactions
  - Adapt to the ever-changing riskiness of banking and near-banking activities
- Illustrative Example: The Glass-Steagall Act of 1933
  - Reflected judgment that underwriting and dealing in corporate securities was riskier than lending
  - But changes in the breadth and depth of the U.S. capital markets after 1933 made it much cheaper for corporations to raise debt in the capital markets than to borrow from official banks
  - As a result, the market for official bank lending shrunk, profits fell and risks soared.

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Too Rigid and Brittle (cont'd)

- Illustrative Example: The Glass-Steagall Act of 1933 (cont'd)
  - Meanwhile, the market for investment (shadow) banking grew, profits soared and risks declined.
  - The investment banks found ways around the restrictions on deposit-taking and money creation through the development of overnight repos, money market funds and securitizations of bank loans
  - These market developments resulted in a flight of talent from the official banks to the investment banks
  - These developments made the 1999 partial repeal of Glass-Steagall inevitable as early as 1980

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Too Rigid and Brittle (cont'd)

- Illustrative Example: The Glass-Steagall Act of 1933 (cont'd)
  - Moreover, because investment banks accounted for such a large share of the U.S. financial system by 2008:
    - U.S. authorities felt they had no choice but to bail them out to prevent contagion and a potential collapse of the U.S. financial system
    - Lehman was the exception that proves the rule

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Too Rigid and Brittle (cont'd)

- The 2008 Financial Crisis and Shadow Banks
  - Recall that during the financial crisis most of the largest financial institutions that had to be rescued were shadow banks:
    - Fannie Mae and Freddie Mac
    - Investment banks like Bear Stearns, Lehman Brothers and Merrill Lynch because of the run on repo
    - Money market funds
    - Commercial paper conduits and other securitization vehicles
    - AIG because of the run on cash collateral and margin demands
    - Official banks whose business models were highly interconnected with shadow banks, such as Countrywide, Golden West (Wachovia), Indymac and Washington Mutual

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banking

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Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Divert attention and resources away from genuine cures

- Genuine cures regulate risk-taking in the overall financial system
  - Directly and flexibly, and not by inflexible proxies
  - Both the official and shadow banking systems
- Examples of genuine cures were recently outlined by former Bank of England Deputy Governor Paul Tucker:
  - Eliminate excessive leverage by increasing capital requirements
  - Eliminate excessive asset / liability mismatch by increasing liquidity of assets or reducing maturity mismatch
  - Eliminate excessive opacity, such as through transparent stress testing
  - Reduce excessive interconnectedness with CCPs and margin
  - Develop credible resolution infrastructure and strategies for all financial institutions

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Divert attention and resources away from genuine cures (cont'd)

- How separation proposals divert attention and resources away from genuine problems and cures:
  - Focus almost all attention and resources on official banking system
  - Like a magician's sleight of hand, blind public and policymakers to similar risks in the shadow banking system
  - The official banking sector is subjected to heavy regulation
  - In contrast, the shadow banking system is left to be regulated like the Wild West – almost anything goes.
  - Results in over-regulation of official banks and under-regulation of shadow banks

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Divert attention and resources away from genuine cures (cont'd)

- Creates competitive advantage for shadow banks
  - Allows the shadow banking system to grow relative to the official banking sector
  - Relegates official banking sector to a smaller and smaller piece of the financial system pie

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Divert attention and resources away from genuine cures (cont'd)

- Well-respected and well-meaning people like Paul Volcker justify separation proposals on ground that official banks are special
  - Just need renewed commitment to allow shadow banks to fail, no matter how much market share they have or what the consequences might be to the financial system or wider economy
  - Totally unrealistic
- Vickers is based on the same premise about the value of separating ring-fenced local retail banks from international investment banking affiliates
  - International arms will be allowed to fail, no matter what the consequences to the global financial system or wider economy
  - Creates regulatory "moral hazard" because home country authorities enjoy domestic benefits of international banking, while shifting most of the costs of failure to host countries

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banking

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Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Will hasten the patient's death

- The patient is the overall financial system
- Illustrative Example: Compare the history of the Glass-Steagall Act to the almost certain fate of the Volcker Rule (or Vickers, Liikanen, etc.)
  - Volcker Rule reflects judgment that proprietary trading, investing in certain funds (and possibly the senior debt securities of securitization vehicles) is riskier than other official bank activities
  - Aside from being demonstrably false, this judgment is unlikely to stand the test of time for the same reason the judgment underlying the Glass-Steagall Act did not
  - The U.S. financial markets are likely to evolve in unpredictable ways that have not been anticipated by the Volcker Rule

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Will hasten the patient's death (cont'd)

- What is now defined as official banking sector will shrink, become less profitable and more risky relative to shadow banking system
- What is now thought to be shadow banking system will grow, become more profitable and less risky relative to official banking system
- Today's shadow banks will figure out practical ways around today's restrictions on deposit-taking and money creation just as they have always done in the past.
- Talent will flee from the official banking sector to the shadow banks

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks

Will hasten the patient's death (cont'd)

- Because shadow banking groups will account for such a large share of the U.S. financial system:
  - U.S. authorities will feel they have no choice but to bail them out when the next crisis hits to avoid contagion and market meltdown, <u>unless</u>
  - Such shadow banking groups are:
    - resolvable without such collateral consequences under:
      - The Bankruptcy Act of 1978, or
      - Title II of the Dodd-Frank Act, and
    - under the same obligation as official banks to
      - prepare resolution plans, and
      - have sufficient loss-absorbing resources and access to liquidity to make such plans credible under severe economic scenarios

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Will hasten the patient's death (cont'd)

- Conclusions
  - By focusing almost all attention and resources on official banking system, the various separation proposals will distort the markets, giving shadow banks an artificial competitive advantage.
  - Over time, this dynamic:
    - Allows the shadow banking system to grow relative to the official banking sector
    - Relegates official banking sector to a smaller and smaller piece of the overall financial system pie
    - Gives the official banking system a powerful incentive and persuasive argument to reduce regulation to level the playing field
      - E.g., reduced capital and liquidity requirements, increased freedom to engage in riskier activities.

Volcker, Vickers, Liikanen, Glass-Steagall, Narrow Banks
Will hasten the patient's death (cont'd)

- Gives shadow banks a powerful incentive to take full advantage of their regulatory advantage by:
  - Further increasing their leverage and decreasing their liquidity relative to the official banking sector
- The net effect is an overall financial system:
  - in which the shadow banking system accounts for a larger and larger share of the pie, and
  - Both the official and shadow banking systems are more leveraged, illiquid and vulnerable to external shocks than they would be without the separation proposals.

- As a result, Volcker, Vickers, Liikanen, Glass-Steagall for the 21st Century and any other Narrow Banking laws and proposals will hasten the death (next financial panic) of the patient (overall financial system), resulting in an increased risk of another round of taxpayer-funded bailouts.

Appendix:
Comparison of Volcker, Vickers, Liikanen

- These slides provide a high-level comparison of the similarities and differences among:[1]
  - the U.S. bank holding company ("**BHC**") structure, pre-Volcker Rule and post-Volcker Rule;
  - the UK banking reform proposal, based on the Vickers report;[2] and
  - the original proposal from the Liikanen Group.

[1] Familiarity with the Vickers and Liikanen proposals and U.S. banking regulation is assumed; many details are omitted here.

[2] The details in this presentation reflect the UK Government's proposal for implementing the Vickers recommendations, as set out in the October 2012 draft banking reform legislation, the policy document accompanying the legislation, and the June 2012 white paper. With respect to some issues addressed here, the UK Government's views diverge from the Vickers recommendations.

Comparison of Volcker, Vickers and Liikanen Proposals

- Key areas for comparison:
  - Deposit-taking
  - Securities underwriting, dealing and trading
  - Intra-group transaction restrictions
  - Geographic restrictions
  - Capital requirements
  - Corporate governance

U.S. Banking Structure – Pre-Volcker Rule*

BANK HOLDING COMPANY

Deposit-Taking Bank

Broker-Dealer or Other Affiliate

Bank-Only Activities

- Deposit-taking (insured and uninsured, from all individuals and all firms)

Permitted Activities

- Lending (consumer and otherwise)
- Underwriting, dealing and trading in U.S. *government and agency* securities
- Buying and selling investment grade and other liquid *debt* securities (including corporates)
- Private placement and brokerage of securities
- FX, currency trading
- Securities lending
- Derivatives brokering, dealing and trading
- Trading in money market instruments (e.g., repos, commercial paper)
- Registered fund advising
- Severely limited sponsoring of registered and private funds
- Some insurance agency activities
- Payment services

Nonbanking Activities

- Underwriting and dealing in *debt and equity* securities
- Merchant banking (*i.e.*, private equity investments), including through private funds
- Insurance underwriting
- Insurance agency activities
- Sponsoring registered and private funds
- Futures commission merchant
- Buying and selling underlying commodities as a complement to trading commodity contracts
- ***No deposit-taking***

23A

23B

Intra-group limits

(quantitative and qualitative limits on credit exposure, asset purchases, provision of services)

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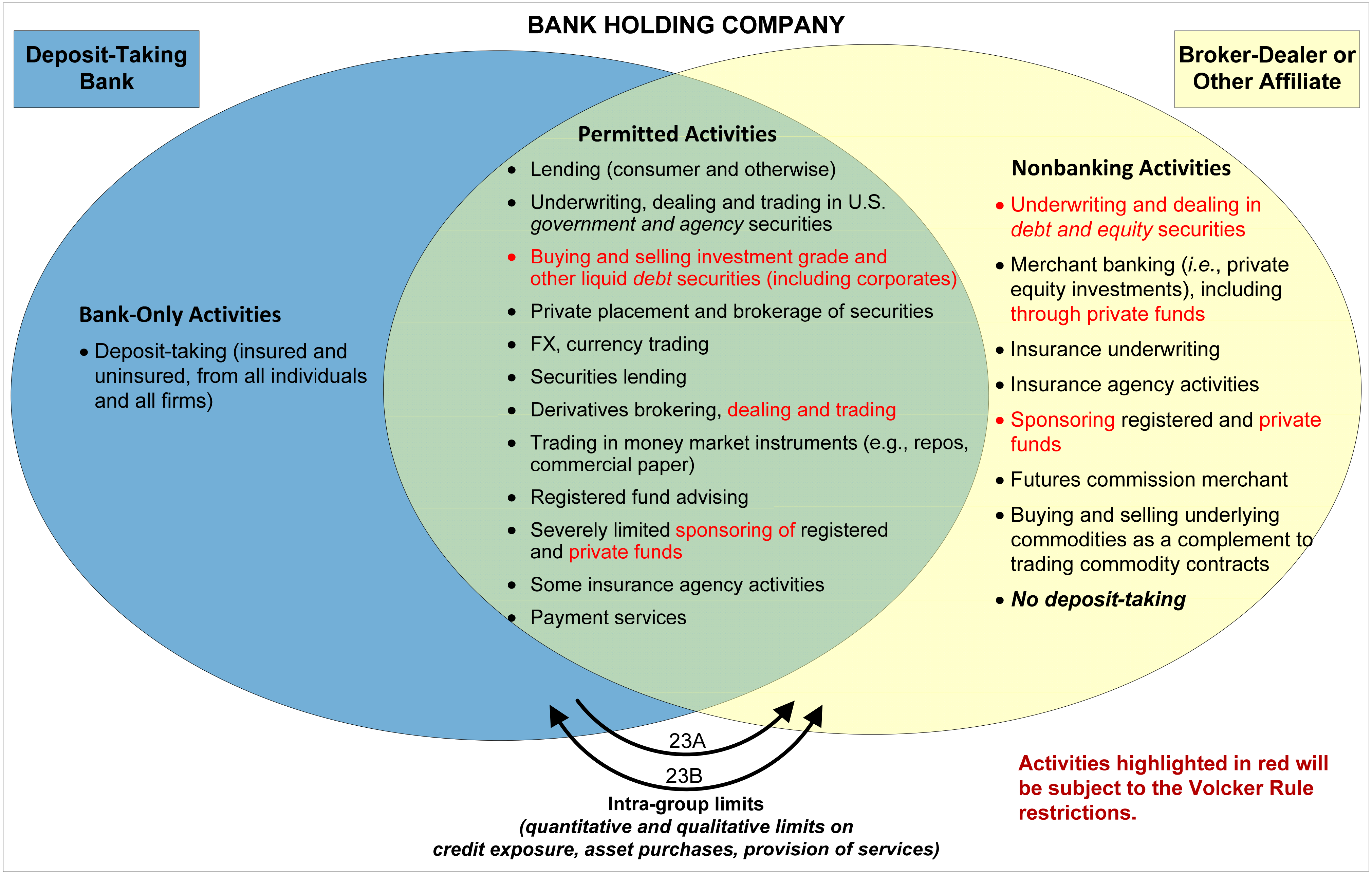
* Information on this slide is presented at a high level of generality. Many details are omitted.

U.S. Banking Structure – Post-Volcker Rule*



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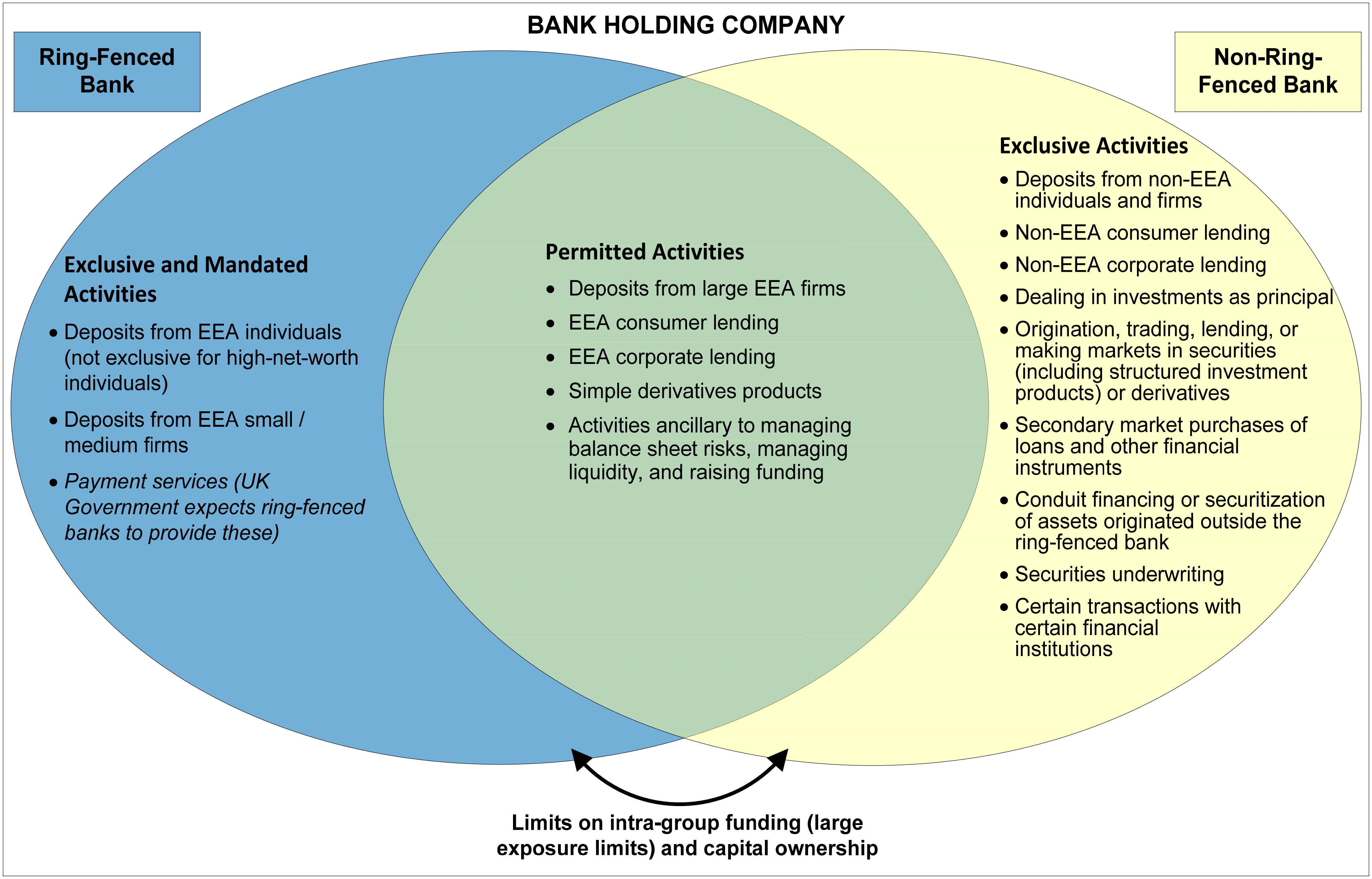
UK Proposal (Vickers)*



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* Information on this slide is presented at a high level of generality based on the proposal. Many details are omitted or are not yet available.

Liikanen Proposal*

BANK HOLDING COMPANY

Deposit Bank

Exclusive Activities

- Retail payment services
- Funding from insured deposits

Permitted Activities

- Consumer and corporate lending
- Trade finance
- Mortgage lending
- Interbank lending
- Loan syndication participation
- Plain vanilla securitization for funding purposes
- Private wealth and asset management
- Exposures to regulated money market funds
- Derivatives trading for own asset and liability management purposes
- Sales/purchases of assets to manage assets in the liquidity portfolio
- Securities underwriting
- Limited hedging services to non-bank clients

Trading Entity

Exclusive Activities

- Proprietary trading of securities and derivatives
- All assets or derivatives positions incurred in market-making
- Loans, loan commitments, unsecured credit exposures to hedge funds / SIVs / similar entities
- Prime brokerage for hedge funds
- Private equity investments
- *Possibly can take uninsured deposits (not clear from proposal)*

Limits on transfers of funding or risk (large exposure limits)

Other Recommendations

- Independent governance
- Bail-in debt
- Executive compensation limits
- Activities permitted for deposit bank can be further limited by recovery and resolution plans

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* Information on this slide is presented at a high level of generality based on the proposal. Many details are omitted or are not yet available.

Deposits

Deposits			
U.S. Pre-Volcker Rule	**U.S. Post-Volcker Rule**	**UK Proposal (Vickers)**	**Liikanen Proposal**
▪ A bank – an insured bank, if retail depositors are involved – is the only entity in a bank holding company structure that may take deposits. ▪ An insured bank may take insured and uninsured deposits, from all individuals and from firms of all sizes. ▪ No specific geographic limits on deposit-taking, except for antitrust-style deposit caps on a per-U.S. state basis.	▪ Same as pre-Volcker Rule.	▪ The ring-fenced bank is allowed to take deposits (insured and uninsured) *only* from EEA individuals and EEA small / medium firms. It is the only entity that may take these deposits. ▪ Both the ring-fenced bank and the non-ring-fenced bank may take deposits (insured and uninsured) from EEA high-net-worth individuals and larger firms. ▪ Only the non-ring-fenced bank may take deposits from non-EEA individuals and firms.	▪ Insured deposits may be taken only in the deposit bank, with no limits on the type of depositor or geographic scope. ▪ The trading entity cannot take insured deposits, but appears to be permitted to take uninsured deposits.

Securities Activities

Securities Underwriting, Dealing and Trading

U.S. Pre-Volcker Rule	U.S. Post-Volcker Rule	UK Proposal (Vickers)	Liikanen Proposal
▪ An insured bank may underwrite and deal only in U.S. government and agency and a limited set of other securities, but may buy and sell investment grade and other liquid debt securities (including corporates), as well as equity and debt securities for bona fide hedging purposes, subject to certain conditions. ▪ A broker-dealer affiliate may underwrite, deal and trade in all debt and equity securities. ▪ As a practical matter, the broker-dealer affiliate handles the securities underwriting activities in most BHCs.	▪ Same as pre-Volcker Rule for underwriting and dealing of U.S. government and agency securities by insured bank. ▪ All underwriting, dealing and trading of non-U.S.-government debt and equity through a "trading account" of an insured bank or any affiliate in a BHC structure must be conducted pursuant to the conditions of certain "permitted activities" (e.g., underwriting and market-making related activities, hedging, trading "on behalf of customers"). ▪ All sponsorship of, investment in and relationships with hedge funds and private equity funds must also be conducted pursuant to a "permitted activity."	▪ The ring-fenced bank is prohibited from underwriting any type of securities. ▪ The non-ring-fenced bank may underwrite all types of securities.	▪ The deposit bank and the trading entity may underwrite all types of securities.

The Glass-Steagall Act of 1933 prohibited affiliations between insured banks and companies "engaged principally" in underwriting and dealing in corporate debt or equity securities. As shown above, however, underwriting, dealing and trading activity occurs in different entities in the bank holding company in the current models. None represents a return to Glass-Steagall.

Intra-Group Restrictions

Intra-Group Restrictions			
U.S. Pre-Volcker Rule	**U.S. Post-Volcker Rule**	**UK Proposal (Vickers)**	**Liikanen Proposal**
▪ Covered transactions between an insured bank and any non-bank affiliate, including asset purchases and credit exposures, are limited to 10% of the bank's capital stock and surplus for transactions with a single affiliate; and a 20% aggregate limit for all covered transactions with all affiliates. ▪ Exemptions exist, such as for intraday extensions of credit, or credit exposures fully secured by cash or U.S. government securities. ▪ Loans and certain other transactions must be adequately collateralized at the time of the transaction. ▪ The Federal Reserve may grant exemptions from the 23A limits; see, e.g., the 2008 waiver of limits on collateralized loans to banks' broker-dealer affiliates. ▪ Under 23B, transactions and services between an insured bank and any non-bank affiliate generally must be on market terms.	▪ Same limits as pre-Volcker Rule, but the Dodd-Frank Act expanded the scope of transactions that are subject to limits, among other changes. ▪ All transactions that are required to be collateralized must be adequately collateralized *at all times*. ▪ Expanded scope of covered transactions, definition of affiliate. ▪ Exemptions require the approval of the Federal Reserve and the bank's primary federal banking regulator based on certain qualitative conditions and are subject to a veto by the Federal Deposit Insurance Corporation.	▪ There are limits on payments from the ring-fenced bank to other members of the banking group and on funding to the ring-fenced bank from the rest of the group. ▪ Intra-group transactions must be on market terms and are subject to large exposure limits, *i.e.*, 25% of regulatory capital, with recommended additional limits on intra-group secured exposures and the quality of their collateral. ▪ The ring-fenced bank may not own or hold the capital of non-ring-fenced affiliates. ▪ The ring-fenced bank cannot use non-ring-fenced banks to access business-critical UK payment systems. ▪ Possible limits on intra-group guarantees, cross-default clauses and derivative netting agreements.	▪ Transfers of risks or funds between the deposit bank and the trading entity must be on market-based terms. ▪ Transfers are subject to the large exposure limits for interbank transactions. ▪ Direct or indirect transfers of risks or funds from the deposit bank to the trading entity are not permitted if capital adequacy would be jeopardized.

Geographic Restrictions

Geographic Restrictions			
U.S. Pre-Volcker Rule	**U.S. Post-Volcker Rule**	**UK Proposal (Vickers)**	**Liikanen Proposal**
▪ There are no effective geographic limits on an insured bank's customer base or activities. ▪ Although some historical geographic restrictions formally remain in the form of interstate banking limits and deposit caps, they do not impose significant limits on the insured bank's activities. ▪ Insured banks and their affiliates may engage in certain activities outside the United States that they may not engage in domestically.	▪ Same as pre-Volcker Rule.	The ring-fenced bank: ▪ Is limited to serving EEA customers and providing services in the EEA; ▪ Cannot carry out any banking activities through non-EEA subsidiaries or branches; and ▪ Can have non-EEA counterparties and hold non-EEA assets if these activities would not impede the bank's resolution.	▪ There are no geographic limits on the deposit bank's customer base or activities.

Capital Requirements

Capital Requirements			
U.S. Pre-Volcker Rule	**U.S. Post-Volcker Rule**	**UK Proposal (Vickers)**	**Liikanen Proposal**
▪ The insured bank and the holding company must separately meet Basel capital requirements. ▪ The broker-dealer affiliate is not required to meet Basel capital requirements on a standalone basis; separate capital requirements are set out by the SEC (including a recent proposal for increased minimum net capital for the largest broker-dealers).	▪ Basel III implementation in progress at an uncertain pace. ▪ The broker-dealer affiliate is not required to meet Basel capital requirements on a standalone basis; separate capital requirements are set out by the SEC (including a recent proposal for increased minimum net capital for the largest broker-dealers).	▪ The ring-fenced bank must meet capital and liquidity requirements under CRD IV and CRR on a standalone basis. ▪ All ring-fenced banks must hold an additional 3.5% of primary loss-absorbing capacity above Basel III standards. ▪ Large ring-fenced banks must hold an additional 3% equity "ring-fence buffer" on top of the Basel III standards, but this will not be in addition to a G-SIB surcharge.	▪ The deposit bank and the trading entity must separately meet capital requirements under CRD IV and CRR. ▪ The Group recommended higher capital requirements for the trading book and real estate lending and suggested that the EC assess whether the expected proposed amendments to the Basel trading-book capital requirements are sufficient to address the risks of the deposit bank and the trading entity.

Corporate Governance

Corporate Governance			
U.S. Pre-Volcker Rule	**U.S. Post-Volcker Rule**	**UK Proposal (Vickers)**	**Liikanen Proposal**
▪ The insured bank is a separate legal entity. ▪ Boards of directors of U.S. banks and bank holding companies are subject to limited independence requirements imposed by banking regulators, and, where applicable, the SEC and securities exchanges. ▪ See, e.g., audit committee independence requirements.	▪ Largely the same as pre-Volcker Rule. ▪ Post-Dodd-Frank changes include a new independent risk committee requirement for large, publicly traded bank holding companies.	▪ The ring-fenced bank must be a separate legal entity, except for banks with £25 billion or less in individual and SME deposits. ▪ The board of the ring-fenced bank must be independent, with at least half the members, excluding the Chair, being independent. ▪ The Chair must be independent upon appointment. ▪ No more than one-third of the ring-fenced bank's board may be representatives of the rest of the banking group. ▪ The directors of the ring-fenced bank and its parent will have an additional duty to protect the ring-fence.	▪ The deposit bank must be a separate legal entity if the activities to be separated are a significant share of the bank's business or if their volume is significant in terms of financial stability. ▪ The proposal recommends a general strengthening of banks' boards and management. ▪ The Group considered a requirement that the boards and governance of the deposit bank and the trading entity be independent of each other, but did not explicitly include this in the proposal.