Big Banks Oppose Volcker Rule, Urge Delay in Implementing It

The deadline for comments on the proposed Volcker Rule was Monday night and hundreds, if not thousands, of letters arrived at the last minute to rail against the rule, mostly from Wall Street. The Volcker Rule — which would prohibit banks from trading with their own money — was proposed last summer by former chairman of the Federal Reserve Paul Volcker, who said in a letter to President Obama that they shouldn't be gambling with money guaranteed by the taxpayers. Big losses by government-backed banks that were trading in risky securities such as mortgage-backed assets precipitated the financial crisis in 2008 and set up the need for federal bailouts of those banks.

The idea behind the rule is simple: Prohibit banks from making "proprietary trades" that are unrelated to traditional banking practices such as making loans and clearing checks. Putting such rules down on paper however is proving to be daunting and giving the banks affected a chance to buy some time.

Volcker's letter to President Obama was three pages long. The rule incorporated into the Dodd-Frank act was 10 pages long. By the time the four regulatory agencies empowered to oversee its implementation — the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve, the Comptroller of the Currency, and the Securities and Exchange Commission (SEC) — got done with it, the Volcker Rule encompassed 298 pages.

The public comment period started when the FDIC signed onto the bill on October 11, and ended Monday, February 13 at midnight. The draft offered for comment contained 1,300 questions on 400 topics so that the agencies would be able to "discern" the right, proper, and appropriate course of action to take with the final draft. Implementation of the Volcker Rule is scheduled for July. This gave the banks a perfect opportunity to delay the whole process by complaining among other things that the bill is far too complicated for the banks to be able to comply by then.

As of Monday the SEC had already received over 14,000 letters, at least one of them 365 pages long. Some attempted to respond to all 1,300 questions with answers of their own while others posed new questions and offered significant revisions to the bill's language.

But that was Monday. By midnight another 200 letters from the primary target of the bill — Wall Street banks and investment houses — were expected. Lawyers representing Goldman Sachs, Morgan Stanley, and Citigroup as well as the trade group itself, the Securities Industry and Financial Markets Association (SIFMA), spent the weekend holed up in hotels in downtown Manhattan cranking out long and detailed responses to the proposed bill.

The strategy is clear: Delay the matter until after the elections when the entire game could change, including the need to reintroduce the legislation for congressional and presidential review, probably with many new faces perhaps more favorable to tabling the matter altogether. Dennis Kelleher, president of Better Markets, a nonprofit pro-regulation group, said, “It’s part of their ongoing strategy — if you can’t kill the rule, you may as well delay it as long as possible.”

From the enormous pushback being engineered by Wall Street, it can safely be assumed that trading with taxpayer-guaranteed funds is a very profitable activity, and the Volcker Bill has the potential for seriously impeding if not eliminating that revenue stream altogether. Delay would allow the affected firms to pony up political contributions in time for the election to influence outcomes favorable to the retention of their power.

Missing from the conversation is how simple such matters would be if left to the private market. Classical economics would call for those bearing the risks to suffer the consequences. If a bank or trading company suffered losses, they would suffer the consequences and change their behavior or go out of business. The free market is brutally effective that way. But it would solve any perceived problem of “proprietary trading” quickly, efficiently, and inexpensively. Government, in its proper role, would serve merely to enforce the laws of contract against fraud. The market would do the rest.

Photo: the Securities and Exchange Commission (SEC) headquarters building