DATA DISPATCH

For biggest U.S. banks, Volcker rule rewrite a 'shoulder shrug,' experts say

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While revisions to the Volcker rule are viewed by banks as a step in the right direction, experts said the rewrite's actual impact on the industry, especially for large institutions, will be muted.

The new rule, approved on Aug. 19 by the Federal Deposit Insurance Corp. and the Office of the Comptroller of the Currency, keeps the stiffest standards in place for big banks and applies only modest changes to smaller banks.

The Volcker rule is a set of regulations put in place after the financial crisis that aims to limit banks' risky trading activities. The rule, finalized in 2013, was almost immediately slammed by industry groups for being too onerous on institutions that engage in relatively minor levels of trading.

"Directionally, this [rewrite] is a win for the industry," said Adam Gilbert, financial services advisory regulatory leader at PricewaterhouseCoopers. "They've been pushing for this for a long time."

But while the rewrite is a net positive for the banking industry, the biggest banks are still required to follow a slew of rules that restrict trading activities, leaving operations at those banks largely unaffected, said Kara Ward, a Washington-based lawyer and partner at Holland & Knight, in an interview.

Things like proprietary trading are still prohibited, while reporting, documenting and supervisory oversight are still required for the largest firms.

"For the biggest banks, it's sort of a shoulder-shrug," Ward said. "Since they're still subject to market risk compliance measures ... it's roughly about the same."

Still, big banks are claiming the revised rule as a win because it provides needed clarity on what the rules actually are and what their scope is.

"The final rule adopted a set of requirements that's more manageable and more aligned with what the regulators will need to satisfy their oversight supervisory responsibilities," Kevin Fromer, CEO of the Financial Services Forum, said in an interview.

The Financial Services Forum is a Washington-based lobbying group that represents eight of the biggest banks in the U.S. Sean Campbell, the Forum's director of policy research, said the improvements in clarity will help banks "know where they stand."

"It will at least have the potential to improve our members' ability to intermediate capital markets activities for their clients," Campbell said.

Another win for the industry, Campbell said, was the removal of the so-called "accounting prong" that was part of the 2018 proposed revision. The accounting prong was criticized by the banking industry as being overly complex. Instead, the final rule will simplify the current "short-term intent prong."

One of the most notable changes in the final rule is its refocus on banks' trading assets and liabilities. The 2013 rule applied to all banks with $50 billion or more in total consolidated assets; the revision replaces that applicability with a three-tier regulatory framework based solely on trading activity, represented by the total dollar amount of trading assets and liabilities.

"[The rule] doesn't open up brand-new customers who want to do this kind of trading," Ward said. "However, if they sort of have more interesting relationships [with hedge funds or private equity funds], they may take those opportunities if they stay under the caps."

The first tier applies to banks with $20 billion or more, which is higher than the $10 billion threshold regulators originally proposed; the second tier applies to banks with assets between $1 billion and $20 billion; and the third tier applies to banks with less than $1 billion in trading assets and liabilities.

An S&P Global Market Intelligence analysis confirms Federal Deposit Insurance Corp. research that banks in the top tier hold about 93% of the trading assets and liabilities in the U.S. banking system. The first and second tiers combined hold about 99% of trading assets.

Only 10 banks would fall into the top-tier category, representing $2.683 trillion in trading assets and liabilities, according to the analysis.

US banks by Volcker rule compliance programs

Trading assets and liabilities tier	Significant (>$20B)	Moderate ($1B-$20B)	Limited (<$1B)
Compliance	*Six-pillar compliance program, annual CEO attestation, and metrics requirements*	*Simplified compliance program*	*Presumption of compliance*
Number of banks	10	24	128
Total assets ($B)	11,571.75	4,542.89	3,879.50
Trading assets + liabilities ($B)	2,683.09	178.13	9.93
Trading assets + liabilities (%)	93.4	6.2	0.3

Data compiled Aug. 28, 2019.
Analysis limited to currently operating top-tier operating U.S. banks and thrifts with at least $10 billion in total assets as of June 30, 2019, or the middle-tier or ultimate parent with greater than $10 billion in total assets for the most recent quarter. Excludes industrial banks, nondepository trusts and banks with a foreign banking organization charter.
Data based on regulatory filings and other publicly available filings for parent's total assets.
Source: S&P Global Market Intelligence

For smaller banks with relatively smaller amounts of trading assets and liabilities, the rule helps lift burdensome restrictions, said Michael Lewis, a financial services attorney and partner at Sidley Austin LLP.

"Some of the biggest winners here are the smaller and more regional banks that don't have as robust trading desks," Lewis said. "It significantly narrows the number of institutions that are subject to the most stringent requirements," he said.

Only 24 banks would land in the second tier, according to the S&P Global Market Intelligence analysis.

Holland & Knight's Ward said the level of trading activity at those banks is extremely low compared to larger institutions. And because the regulations are both tailored and less strict, smaller banks' compliance departments can breathe easier, she said.

"Depending on their sophistication and how tough they are, very few of them are going have anything close to those trading assets and liabilities," Ward said. "This is a big help for those banks who haven't engaged in any of that kind of activity."

Banks in the first tier are subject to a "six-pillar" compliance program that includes documented procedures and processes for trading, trading metrics disclosures and an annual letter from the CEO confirming that the bank is in compliance. In the second tier, a far less complicated compliance program is required, potentially freeing up a number of bank personnel and providing significant savings, Ward said.

US banks by most trading assets and liabilities

Company (top-level ticker)	City, state/province	Total assets ($B)	Trading assets + trading liabilities ($B)	Trading assets + trading liabilities as a % of total assets (%)	as a % of total assets YOY change (pps)
JPMorgan Chase & Co. (JPM)	New York, NY	2,727.38	670.77	24.6	2.6
Goldman Sachs Group Inc. (GS)	New York, NY	944.92	455.52	48.2	3.3
Citigroup Inc. (C)	New York, NY	1,988.23	440.69	22.2	1.2
Bank of America Corp. (BAC)	Charlotte, NC	2,396.48	423.15	17.7	1.1
Morgan Stanley (MS)	New York, NY	891.96	384.43	43.1	1.8
Wells Fargo & Co. (WFC)	San Francisco, CA	1,923.39	129.51	6.7	-0.1
HSBC North America Holdings Inc. (HSBA)	New York, NY	296.71	65.06	21.9	2.3
Credit Suisse Holdings (USA) Inc. (CSGN)	New York, NY	128.61	46.08	35.8	10.6
DB USA Corp. (DBK)	New York, NY	119.75	35.90	30.0	2.6
Barclays US LLC (BARC)	New York, NY	154.33	31.99	20.7	-4.6
RBC US Group Holdings LLC (RY)	Toronto, Ontario	125.58	18.70	14.9	-9.3
Mizuho Americas LLC (8411)	New York, NY	46.92	17.54	37.4	-2.8
TD Group US Holdings LLC (TD)	Wilmington, DE	387.66	16.84	4.3	-2.1
BMO Financial Corp. (BMO)	Chicago, IL	160.25	15.07	9.4	2.3
MUFG Americas Holdings Corp. (8306)	New York, NY	172.01	14.70	8.5	-2.2
UBS Americas Holding LLC (UBSG)	New York, NY	135.55	14.39	10.6	-5.1
BNP Paribas USA Inc. (BNP)	New York, NY	129.37	13.45	10.4	-1.4
Bank of New York Mellon Corp. (BK)	New York, NY	381.21	11.80	3.1	0.3
State Street Corp. (STT)	Boston, MA	241.54	8.77	3.6	-1.1
SunTrust Banks Inc. (STI)	Atlanta, GA	222.53	7.82	3.5	0.2

Data compiled Aug. 28, 2019.
Analysis limited to currently operating top-tier U.S. banks and thrifts. Excludes industrial banks, nondepository trusts and banks with a foreign banking organization charter.
Data based on regulatory filings and other publicly available filings for parent's total assets.
Tickers based on top-level entities' home country stock exchanges.
Source: S&P Global Market Intelligence

But getting to the final rule was not easy for regulators, who had to walk a fine line between restricting risky trades that contributed to the financial crisis and relieving overly burdensome rules.

The end result is a more "objective standard" that places the onus on banks to decide whether they will trade or not, Raymond James' Mills said. And that activity determines which regulatory tier will govern it.

"The push here is: We want to preserve the regulation for the money-center banks, and for the smaller banks, completely get them out," Mills said. "I would almost argue that it was a drafting error that all banks would have to comply with the Volcker rule to begin with."

Regulators' goal, as stated by FDIC Chair Jelena McWilliams, was to "provide more clarity, certainty, and objectivity around the Volcker Rule, while tailoring the requirements to focus on those banks that conduct the overwhelming majority of trades."

Fears that the Volcker rule will be repealed or defanged, which will allow an overwhelming number of risky trades to precipitate another financial crisis, are misplaced, Sidley Austin's Lewis said.

"The core of the rule, the basic prohibition on [proprietary] trading and the basic prohibition on certain covered fund activities remains in place," Lewis said. "I think people that have suggested that 'they've repealed the Volcker rule,' [are exaggerating]."

The three other banking regulators in charge of the Volcker rule — the Securities and Exchange Commission, the Federal Reserve and the Commodity Futures Trading Commission — will also have to sign off on the interagency effort in order for it to take effect.

Harry Terris contributed to this article.

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