Obama’s ‘Volcker Rule’ May Not Survive Congressional Skepticism

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By Alison Vekshin
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President Barack Obama’s “Volcker Rule” to ban proprietary trading at U.S. banks may not survive in Congress, hampered by criticism that the administration waited too long and offered too few details.

The proposal’s timing is viewed by some as “transparently political and not substantive,” Senate Banking Committee Chairman Christopher Dodd said on Feb. 2. It was “airdropped” into the Senate debate on legislation to overhaul U.S. financial rules, said Senator Richard Shelby, the panel’s top Republican.

“It’s tough to take on another issue at this point,” Dodd, a Connecticut Democrat, said at a hearing in Washington yesterday that included executives from Goldman Sachs Group Inc. and JPMorgan Chase & Co. “It was never my intention, or I believe the intention of this committee, to solve every issue surrounding the financial-services sector.”

Members of the Senate panel have been working for weeks to translate into legislation the plan Obama released in June to overhaul U.S. financial rules. The focus is on the Senate after the House passed its version of the legislation in December.

Obama named the Jan. 21 proposal after its chief proponent, ex-Federal Reserve Chairman Paul Volcker, now a White House adviser. Based on an idea circulated in a January 2009 report by the Volcker-led Group of Thirty, composed of former central bankers and finance ministers, it would force banks to stop the trading they do on their own accounts and give up their stakes in hedge funds and private-equity funds.

**Citigroup Trader Quits**

Some traders have already taken note. Matthew Carpenter, head of a Citigroup Inc. unit that trades U.S. stocks using the bank’s money, quit to join hedge fund Moore Capital Management LP, people briefed on the matter said yesterday. Leaving with him is his deputy, Matthew Newton, amid concern the government may order banks to exit such businesses, the people said.

Dodd and Shelby told reporters yesterday they hadn’t ruled out incorporating the plan into the bill. Dodd, who on Feb. 2 said he “strongly” supported the proposal, said he’d consider language empowering regulators to carry out the recommendations without having lawmakers write the rules, and Shelby said he wanted to see whether regulators already have the power.

The announcement came two days after a Republican victory in the Massachusetts Senate race that cost Democrats their supermajority in the Senate -- timing that stoked speculation it was motivated by politics.
Volcker said Feb. 2 that the timing was “sheer coincidence.” Obama decided to back the proposal weeks before the Massachusetts election, he said. Volcker wasn’t available for comment yesterday, according to his assistant, Anke Dening.

**Client Business**

The White House defines proprietary trades as those not done for the benefit of customers, a senior administration official said when the Volcker plan was announced. Regulators would have the power to ask banks whether certain trades are related to client business, the official said. If they’re not, the regulators could order firms to exit the positions.

“We’re working closely with the Congress to rein in risky practices on Wall Street,” Treasury Department spokesman Andrew Williams said in an e-mailed statement. “The House passed a strong bill in December and now we’re working with the Senate to get the job done.”

Senator Michael Crapo, an Idaho Republican, pressed Deputy Treasury Secretary Neal Wolin at the Feb. 2 hearing to release details of the plan “so that we can understand specifically what we are talking about or what the proposal is with regard to proprietary trading.”

Wolin responded by telling Crapo the administration is working with regulators to prepare a draft legislative proposal that it will send to Congress “soon.”

**Drawing a Line**

Drawing a line between bank and customer trading won’t be easy, said Hal Scott, a professor at Harvard Law School who specializes in international financial systems.

A narrow definition probably won’t reduce risk, Scott said, while a broad one could “seriously impair the basic function of modern banks as market-makers” in government and non-government securities and as packagers of consumer debt into bonds.

Goldman Sachs’s E. Gerald Corrigan, who like Volcker is a past president of the Federal Reserve Bank of New York, said at yesterday’s hearing that banks should be allowed to own and sponsor hedge funds and private equity funds because any risks can be managed. Corrigan is chairman of the firm’s regulated bank subsidiary.

Barry Zubrow, JPMorgan’s chief risk officer, told the committee the activities the administration is proposing to restrict didn’t cause the financial crisis.

“Indeed, in many cases, those activities diversified financial institutions’ revenue streams and served as a source of stability,” Zubrow said in his prepared testimony. “Further, regulators currently have the authority to ensure that risks are adequately managed in the areas the administration proposes to restrict.”

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