Fed eases "Volcker Rule" limits on bank speculation

By Patrick Martin
1 June 2018

The Federal Reserve Board, the principal US bank regulator, approved plans Wednesday to loosen restrictions on high-risk trading conducted by the major banks, after intensive pressure by Wall Street and the Trump administration.

The Fed decision does not repeal the so-called Volcker Rule, named after the former Fed chairman, Paul Volcker, who helped devise it after the crash. But it significantly reduces the compliance burden for the biggest banks, while exempting many smaller banks entirely.

Fed Chairman Jerome Powell declared Wednesday, "Our goal is to replace overly complex and inefficient requirements with a more streamlined set of requirements." Four other bank regulatory institutions must approve the proposed changes, including the Federal Deposit Insurance Corporation (FDIC) and the Commodity Futures Trading Commission, and there will be a 60-day period for public comment before the new rules become final.

Based on that timetable, it appears likely that by the time the tenth anniversary of the September 2008 crash rolls around, the banks will have been effectively released from even cosmetic restrictions on the kind of speculative trading that produced the biggest financial catastrophe in history.

The supposed purpose of the Volcker Rule was to prevent banks from using ordinary deposits, guaranteed by the FDIC, to engage in speculative trading, particularly in highly leveraged markets like those for derivatives and other extremely complex financial instruments. In effect, the banks were making risky gambles to get quick superprofits, with the assurance that the taxpayers would pick up the tab if the bets went sour.

The most important change approved Wednesday by the Fed shifts the burden of proof. Banks were previously required to show that each trade with FDIC-insured funds was in response to a customer demand or as a hedge against specific risks, rather than "proprietary," i.e., for speculative purposes. Now such trades will be presumed valid based on the banks establishing compliance programs tailored to the requirements of the Volcker Rule.

Chairman Powell announced the unanimous vote by the Fed, including its remaining Democratic appointee, Lael Brainard, who issued her own statement supporting the action, seeking to present it as a more efficient execution of the Volcker Rule, rather than its gutting. "The premise of the Volcker Rule is compelling," Brainard said. "Banks should not engage in speculative trading activity for which the federal safety net was never intended."

The Fed move follows less than a week after President Donald Trump signed into law a partial rollback of the Dodd-Frank banking legislation, which provided the legal basis for the Volcker Rule. That bill passed the House and Senate by comfortable margins with large numbers of Democrats joining nearly all Republicans in voting for the legislation.

These measures were imposed after the Wall Street crash in a cosmetic effort by congressional Democrats and the Obama administration to disguise the trillion-dollar bailout of the banks as part of an effort at "reform" of the financial system to prevent future crashes.

With the dismantling of the pretense of bank regulation, the bailout can be seen for what it was: a brazen handout of trillions of dollars in taxpayer funds to the biggest financial institutions, including banks, hedge funds and brokerage houses, to preserve the capitalist system and the wealth of the financial aristocracy, at the expense of working people.

Despite the moaning and whining by bank CEOs and lobbyists about the supposed restrictions imposed by the Dodd-Frank law and regulations like the Volcker Rule, bank profits soared to a record $56 billion during the first quarter of 2018.

The banking lobby hailed the Fed action, claiming it reflected “the growing recognition by policymakers of the unintended negative impact due to the excessive complexity of the current regulations,” said Kenneth E. Bentsen, chief executive of the Securities Industry and Financial Markets Association. Bentsen is a former Democratic congressman and the nephew of the late Senator (and Treasury secretary) Lloyd Bentsen.

The financial industry trade press gloated over the Fed action, with headlines like “Weakened Volcker Rule marks big win for Wall Street.”

The drive to deregulate the financial behemoths who crashed the US and world economy and wiped out tens of millions of jobs, and the life savings of millions more is fully bipartisan, with the backing of most Republicans and a substantial number of Democrats.

The partial repeal of Dodd-Frank passed the US Senate May 16 by 67-31, with 17 Democrats providing the margin of victory. On May 24, the Senate voted by 69-24 to confirm Jelena McWilliams, the chief legal officer of Fifth Third Bancorp, to become chairman of the FDIC, the second most important bank regulator, with 20 Democrats embracing the Trump administration principle that regulatory agencies should be controlled by the industries they are supposed to oversee.