

The Volcker Rule and Regulations of Scope

By Matthew P. Richardson and Bruce Tuckman

A key objective of bank regulation since the financial crisis of 2007-2009 has been to reduce risk. The Volcker Rule, however, regulates the scope of bank activities by prohibiting proprietary trading and severely limiting investments in hedge funds and private equity funds. In our view, the Volcker Rule is too inefficient a means of regulating risk.

First, the prohibitions of the Volcker Rule are not closely aligned with risk. Making and trading corporate loans, for example, is permitted, while investing and trading in corporate bonds or in funds that invest in corporate bonds is prohibited.

Second, compliance with the Volcker Rule is extremely costly. Essentially, because it has proven so difficult to establish clear regulations, banks have been burdened with justifying a massive number of individual trades and investments as permissible.

We support the CHOICE Act's proposal to repeal the Volcker Rule. Risk can be controlled much more efficiently by concentrating bank and regulatory resources on other prudential tools like bank examinations, risk-weighted capital requirements, leverage ratios, liquidity ratios, Living Wills, and stress tests.