

December 15, 2013 5:12 pm

## Lawyers fear uncertainty of UK bank reforms

By Sam Fleming

Britain's banks are heading for the kind of legal wrangling and uncertainty that has dogged the introduction of the Volcker rule in the US, with lawyers warning radical reforms will have unintended consequences.

With the banking reform bill that will create a "ring fence" around high street operations set to become law this week, City lawyers and bankers say there are serious faults in the draft secondary legislation that will contain the details of the reforms.

Like the Volcker rule, the UK ring fence is a beguilingly simple concept; the main point of Volcker is to ban proprietary trading; the UK ringfence separates investment banking from retail activity.

However, one consequence of a ring fence is that small businesses could be left with a much narrower choice of trade finance and derivative products, lawyers say. Costs may also be higher. Small banks may find their ability to do business with big ringfenced counterparts is curtailed.

"The issue is getting something that is workable and that does not throw sand in the wheels of 'good' financial activity, such as trade finance," said Bob Penn, a partner at City law firm Allen & Overy.

"Frankly we are not even at the end of the beginning – the work starts here with the banking reform bill becoming law," he said.

Jan Putnis, a partner at Slaughter and May, another City law firm, said: "It is now up to the industry to put the issues clearly to the government and demonstrate their gravity – that these are issues for customers, not just for the banks."

However he added: "I don't see why this can't be made to work in the long term."

The Independent Commission on Banking – headed by Sir John Vickers – in 2011 recommended ringfencing retail banking activities to protect them from investment banking losses.

Now the banking reform bill is due to have its final day in the House of Lords on Monday, clearing the way for it to become law this week.

Much of the detail of the ring fence will be contained in secondary legislation to be enacted in 2014. The Government's approach has been to "hard wire" as much detail as possible into the bill, to prevent the barrier from being eroded over time.

Some lawyers argue this will lead to an inflexible regime and that it would be better to give the City regulator the power to hammer out the details. While the secondary legislation will contain exceptions to the restrictions on ringfenced banks, important areas will inevitably be missed out, they say.

For example, ring fenced banks will not be able to offer certain basic derivatives products and trade finance services to small businesses, meaning customers may move to smaller banks or UK branches of overseas banks, which will not be subject to ring fencing.

Restrictions on ringfenced banks' exposure to other financial institutions could have unintended consequences – for example it could stop them from being able to buy buildings insurance, according to the British Bankers' Association.

Smaller banks worry that while they will be able to deposit money with ringfenced banks, they will not be able to obtain funding from them.

Government insiders say the secondary legislation still needs to be "refined" but insist the details are close to being sorted out.

The Treasury said: "The government is delivering the biggest ever overhaul of Britain's banking sector to create a stronger and safer system that supports the economy, businesses and consumers . . . We will continue to work closely with the sector and regulators as we finalise the details of these reforms."

Paul Chisnall, an executive director of the BBA, said: "The Volcker rule has shown that what is simple in concept can be challenging to express in law. We face the same phenomenon here."

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