Global Banks Face Increasing Complexity

Knowledge@Wharton: So not only is there a lot of fuzzy math around capital requirements in Basel III alone, but then of course we have the whole new regulatory regime in the U.S. [under Dodd-Frank] and then what the G-20 is doing, and then there are other entities in Europe that are looking at new rules for the eurozone. What kind of coherence or incoherence are we going to see among those rules? We are talking about global banks – they have got to deal with Basel III, but they've also got to deal with Dodd-Frank and they've got to deal with whatever the G-20 comes up with.

Donald Vangel: I think the potential for a very balkanized world around some of these specific rules is legion. I think even within the U.S. what I find really interesting is regulatory reform actually created a more complex regulatory structure rather than a less complex regulatory structure. There are some 250 rules that need to be written – many of them jointly by numerous agencies. The statute in effect gives almost every regulatory agency backup authority over every other regulatory agency, and getting regulators to cooperate and work cohesively that way, in my personal view, has never been a strong suit of the U.S. regulatory environment. And then you look the way issues are evolving as they relate to things like incentive compensation -- where the approach in the U.S. so far has been a somewhat principles'-based approach looking at the way incentive structures are structured – the governance around them as it relates to risk-taking is trying to move the industry towards more discipline. The approach in Europe is much more prescriptive. Institutions that operate globally are going to need to comply with both sets of requirements. I think the fragmentation around the world is likely to be increasingly significant.

Richard Herring: I have a wonderful picture that illustrates your first point. It's by one of the major U.S. banks and it shows the sort of cross-cutting reporting to various regulators for each of their lines of business. And then it shows what Dodd-Frank added. And it virtually doubles the complexity of the system. It's just astonishing. And to think that we are going to deal with all of this through a committee of 10 and hangers on – most of whom have no expertise or interest in systemic risk -- is to me a design for disaster.

Donald Vangel: It is going to be interesting.