U.K. Regulator Holds Firm on Bank Segregation Plan

Ruling sets the stage for more painful restructuring at British lenders

By MAX COLCHESTER, WSJ.com, Updated Oct. 15, 2015 1:55 p.m. ET

LONDON—A **U.K. regulator on Thursday held firm on a law to force banks to segregate their retail and investment-banking operations**, setting the stage for more painful restructuring at British lenders.

**Big U.K. banks are required to separate their retail banks from investment-banking activities by 2019 in a bid to ensure depositors and small businesses aren’t put at risk if a lender’s investment banking operations fail.** On Thursday the Bank of England said the **“ringfenced” retail operations of big U.K. banks would have to hold extra capital to cover risk in their operations**, even if they are part of larger well-capitalized banks.

Despite a wave of lobbying by British banks, the Bank of England stuck to the principals of the project first outlined in 2011 and enacted in law two years ago. Unlike Glass-Steagall, the Depression-era U.S. act that separated securities and banking activities for more than 60 years before being repealed in 1999, the **U.K. rules don’t ban lenders from operating both investment banking and retail activities.**

**The European Union is planning its own version of ringfencing, while Vermont Sen. Bernie Sanders and former Maryland Gov. Martin O’Malley indicated in a Democratic presidential debate this week that they would support reinstatement of the Glass-Steagall Act.**

The U.K.’s central bank offered hints of the complexity involved in running two banks under one holding company. For example, the bank’s retail operations will have to pay market rates for services provided by other parts of the bank. Lenders subject to the rules will need permission from the Bank of England for their retail arms to pay dividends to their parent companies.

One big question remains unanswered: how much capital will be locked up in the ring fenced unit. The central bank’s Financial Policy Committee has yet to determine exactly how much extra capital the six affected banks will need to hold but the regulator said they may need a total of £3.3 billion ($5.12 billion).

The plans, which **affect all British banks with more than £25 billion in deposits**, are in line with expectations, said Steven Hall, banking partner at KPMG. Banks “can pay dividends against a backdrop of capital requirements which are tightening,” he said.

**Barclays PLC, HSBC Holdings PLC, Lloyds Banking Group PLC, Royal Bank of Scotland Group PLC, Co-operative Bank PLC and Santander U.K., the U.K. arm of Spain’s Banco Santander SA will all be impacted by the rules**.

Separately, in a fillip to the industry, U.K. regulators are rowing back on a much criticized rule that would find senior bankers who oversee failed banks guilty until they prove their own innocence. New draft legislation will instead give executives a “duty of responsibility” to guard against failings, and would extend the new regime of personal accountability to all types of financial firms rather than just banks.

Lawyers said the reverse burden of proof clause had made some top bankers wary of joining British banks, since the executives would have had to prove that they had done everything in their powers to prevent any potential regulatory breaches, rather than requiring the regulator to prove that adequate steps hadn’t been taken.

Write to Max Colchester at max.colchester@wsj.com