

Summary

Maintaining the universal banking model - An institutional theory perspective on the endogenization of a transnational post-crisis financial market reform

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Following the discussions on a separation of banking activities in the US and in the UK, in 2012, EU Commissioner Michel Barnier mandated an expert panel (High Level Expert Group) to assess the necessity of a structural banking reform in the EU. This expert panel concluded that, despite the numerous ongoing regulatory initiatives and reforms being implemented so far, a separation of banking activities is indeed necessary (Liikanen report, 2012, p. 100). This recommendation was welcomed by several EU institutions (European Parliament, 2013; European Commission, 2014b) who suggested to separate banking activities, too. However, in the end, no regulation has been established at EU level.

The paper entitled “Maintaining the universal banking model – An institutional theory perspective on the endogenization of a transnational post-crisis financial market reform” analyses the rule-making process regarding the EU structural banking reform which did not lead to any final regulation. The following research questions are raised: What are the rhetorical strategies used in the regulatory arena? What role do national reforms play in the transnational regulatory process? How are the views voiced in the regulatory arena reflected in the regulatory proposals and in the rule-making process?

To address these research questions, we employ the concept of endogenization of law and institutional maintenance work. According to the literature on endogenization of law (Edelman, 1990, 1992; Edelman et al., 2011; Suchman and Edelman, 1996), regulation cannot be regarded as an exogenous force wherein authoritative rules are concrete and determinative but rather as being endogenized by those regulated. Law and organizations are considered as being dynamically intertwined since organizations do not only respond to law but are also active in constructing and configuring legal regimes (see also Edelman and Suchman, 1997). These processes render law endogenous. Regarding the literature on institutional work (e.g. Lawrence and Suddaby, 2006; Lawrence et al., 2009, Maguire et al., 2004; Seo and Creed, 2002), we focus on institutional maintenance which represents one of three types of institutional work.¹ Maintenance work describes the actions of individuals or organizations aiming at institutional continuity and stability. The concept has also been employed by prior literature to illustrate the

¹ The two other types comprise institutional creation and institutional disruption (Lawrence and Suddaby, 2006, p. 215).

successful avoidance of regulatory changes in the post-financial crisis era (Rainelli-Weiss and Huault, 2016; Riaz et al., 2011, 2016; Taupin, 2012).

We adopt a qualitative case study design which is appropriate for analyzing complex, dynamic and value-laden phenomena (Cooper and Morgan, 2008). The structural banking reform can be described as a complex matter because empirical studies have not agreed on a consensus view on the benefits or shortcomings of large and diversified banks (e.g. Berger and Mester, 1997; DeLong, 2001; Stiroh, 2014; Wheelock and Wilson, 2012). The EU structural banking reform represents a dynamic phenomenon, too, since it depends, for example, on the preferences of politicians which may not be constant over time and are potentially influenced by developments in the banking sector or in the wider economy. The reform is also value-laden because it ultimately raises the question on the appropriate role of the supervisor, or in other words, the required degree of state intervention in the banking market.

This study uses a multitude of data sources. In order to better understand the regulatory process, all proposals that have been issued at EU level have been analyzed, namely the Liikanen report published in 2012, the European Commission proposal of 2014, the European Parliament proposal of 2015 as well as the proposal of the European Council published in 2015. In addition, further documents issued by other EU institutions, such as reports from the European Central Bank or the European Banking Authority, and national structural banking reforms have been examined. Furthermore, contextual information was obtained via the media data base Factiva. In addition to the above-mentioned archival documents and press articles, the public consultation which was held by the European Commission from May to July 2013 was analyzed, too. The European Commission received 540 replies, of which 439 by individuals who were either copying or very closely following a comment letter proposed by the NGO Finance Watch (European Commission, 2013). We focus on those letters that were written by public authorities (in particular governments, central banks, regulators) and (registered and unregistered) organizations, comprising for example, banks and bank associations, unions and consumer organizations. More precisely, the analysis builds on 14 comment letters by public authorities, 44 comment letters by registered organizations and 32 comment letters by unregistered organizations. While our analysis does not consider the vast majority of comments that were written by individuals, this is no major limitation given our focus on the argumentative strategies used by key players of the regulatory space (also cf. Bozanic et al., 2012).

The analysis of comment letters by banks revealed three strategies of institutional maintenance work of which two were already introduced by Lawrence and Suddaby (2006).² We label this third strategy contextualizing, i.e. the reference to other regulation that allegedly renders the proposed regulation unnecessary. This strategy, which proves powerful in arguing for the

² These strategies include demonizing, i.e. the presentation of negative examples of possible consequences of the institutional change to underline the normative foundation of the institution, and mythologizing, i.e. highlighting the past glories of an institution. It should be noted that we take up the terminology proposed by Lawrence and Suddaby (2006). The terms are not intended to have normative implications in the sense that these strategies are “inappropriate”.

maintenance of the status quo, in essence highlights the importance of path dependencies and the context in which the specific institutional change is set up. Interestingly, our results show that these strategies were not only employed by addresses of regulation but also by other banks and bank associations as well as public authorities and non-banks providing further legitimacy to the comments of banks.

Furthermore, our case highlights how the transnational dimension influences the maintenance work of actors. By analyzing the regulatory process, we identify a fourth strategy of maintenance work that we label bottom-up enabling work, i.e. the creation of rules by actors from a lower (national) level for the purpose of influencing the institutional change that is expected to happen at a higher (transnational) level. This strategy provided actors with an argument against any further regulation at the EU level and played an important role in the transnational rule-making process. This finding is consistent with Djelic and Quack (2003, p. 306) who argue that the creation of institutions at the transnational level cannot be conceived in absence of the national rules of the game. In our case, this effect is even more pronounced because governments (here: the German and French government) created their national rules with the intent to influence rules at the transnational level (the EU reform).

Finally, we document how the EU proposals have become significantly diluted and progressively more aligned to the status quo indicating a successive endogenization of regulatory proposals. By combining the theoretical perspectives of institutional maintenance work and legal endogenization, this paper acknowledges the role of agency in endogenizing regulation. Thus, we are able to analyze both sides of the regulatory process on banking separation, the institutional maintenance work by banks and others key players in the regulatory arena during the rule-making process and how the views voiced by those actors successively entered the European regulatory proposals. We contribute to the literature employing the concept of endogenization of law (e.g. Alon and Dwyer, 2016; Bozanic et al., 2012; Covaleski et al., 2013; Mulligan and Oats, 2016) by revealing the strategies of institutional maintenance work in the context of a transnational financial market reform in the aftermath of the financial crisis. Our results highlight an iterative interplay between endogenization and institutional maintenance work as endogenization is not only the result of successful maintenance work but is also part of institutional maintenance work itself.

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