

Chapter 7.16

IT Development and the Separation of Banking and Commerce: Comparative Perspectives of the U.S. and Japan

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ABSTRACT

Unlike the UK, Germany, France, and some major countries that permit entries from banking to commerce and vice versa (“two-way” regulation), the United States and Japan have maintained a policy of separating banking and commerce out of concern that the mixing of the two activities would result in the misallocation of credits, anti-competitive effects, exposure of deposit insurance, and taxpayers to greater risks from commerce and additional supervisory burdens on banking and antitrust regulators. However, this separation is now being reconsidered both in the U.S. and Japan. With IT development, linking online banking and Internet commerce may increase profitability through operating synergies between the two firms and reduce average costs and information costs. Future changes in the financial environment

may produce other synergies and the degree of separation should be suitable for such business development. This chapter introduces current laws and discussions in both countries and considers the future of the separation policy in Japan.

INTRODUCTION

The Separation Policy of Banking and Commerce

Unlike the U.K., Germany, France, and some major countries that allow entries from both banking to commerce and vice versa, the United States and Japan have maintained the policy of separating banking and commerce out of concern that the mixing of the two activities would result in bad effects as stated.

According to Brown (2002), “the U.S. has maintained this long-standing policy of separating banking and commerce out of concern that the mixing of banking and commercial activities would result in the misallocation of credit, extensive anti-competitive practices, and exposure of the federal safety net established for banking to a broad range of risks emanating from commercial sectors of the economy. Other concerns posed by the mixing of banking and commerce include overburdening the supervisory resources of the federal banking regulators, consumer privacy problems, and reduction of credit availability in local communities.”

Japanese regulators have similar concerns. Although the indirect ties between main banks and commercial firms under the keiretsu control had been criticized by U.S. trade negotiators, Japanese law had long maintained the strict policy of separating banking from commerce until recently. This structural division between banking and commerce has been codified in the Banking Act¹ and the Antimonopoly Code.² As in the United States, Japan has maintained this separation policy out of concern that the mixing of banking and commercial activities would result in (1) the misallocation of credits, (2) anti-competitive effects, (3) exposure of the deposit insurance and taxpayers to greater risks from commerce, and (4) additional supervisory burdens by banking and antitrust regulators. The United States and Japan both learned from past economic crises (in 1929 in the U.S., in 1927 in Japan) before World War II and created the current system. As a result, banking is heavily regulated and separated from commerce, which is less regulated.

Lifting the Separation?

However, this separation is being reconsidered both in the U.S. and Japan. With IT development, linking online banking and Internet commerce may increase profitability through operating synergies between the two firms, and reduce aver-

age costs and information costs. Future changes in the financial environment may produce other synergies and the degree of separation should be suitable for such business development.

Compared with the strict separation in the U.S.³ except for unitary thrifts, the Japanese government recently allowed “one-way” entry from commerce to banking with some requirements. Actually two recent reforms were introduced to allow commerce to enter into banking with fewer regulatory burdens. First, in August 2000, Japanese financial regulators allowed commercial companies to engage in “Internet” banking and the securities business with fewer requirements than a normal banking business. Second, in April 2006, commercial companies were allowed to become bank agencies by meeting some requirements. As a result, the current Japanese regulation of the separation of banking and commerce is called “one-way”⁴ regulation, which means that commercial companies can start banking businesses but banks are restricted from starting commercial or non-banking businesses of their own and from holding many shares (details are shown later). Compared with Japanese regulation, the U.S. regulation is called “no-way”⁵ regulation, which restricts both entries from banking and commerce. On the other hand, the regulations in the U.K., France, Germany, and other major E.U. countries are called “two-way”⁶ regulation, which permits both entries from banking and commerce.⁷ These trends can also be observed in the World Bank survey (Caprio, G., Levine, R.E., & Barth, J.R., 2001).

Some Japanese bankers insist that Japan should move to “two-way” regulation by permitting banks’ subsidiaries or affiliates to engage in commercial business (e.g., real estate). Before illustrating the situations of both countries, let us observe why banks want to hold commercial shares.

Many promoters in the U.S. and Japan insist that a combination between commerce and banking may enhance profitability through operating

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