118513

BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Chairman Federal Financial Institutions Examination Council

Information About Depository Institutions' Ancillary Activities Is Not Adequate For Policy Purposes

GAO's review of the extent and nature of nonbanking activities of depository institutions showed that current information is not adequate for the Congress and Federal regulators to make needed policy decisions. GAO recommends that the Federal Financial Institutions Examination Council design a means for obtaining the needed information which is consistent with the intent of the Paperwork Reduction Act of 1980.

118513

GAO/GGD-82-57
JUNE 1, 1982

022206

Request for copies of GAO reports should be sent to:

U.S. General Accounting Office
Document Handling and Information
Services Facility
P.O. Box 6015
Gaithersburg, Md. 20760

Telephone (202) 275-6241

The first five copies of individual reports are free of charge. Additional copies of bound audit reports are $3.25 each. Additional copies of unbound report (i.e., letter reports) and most other publications are $1.00 each. There will be a 25% discount on all orders for 100 or more copies mailed to a single address. Sales orders must be prepaid on a cash, check, or money order basis. Check should be made out to the "Superintendent of Documents".

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

GENERAL GOVERNMENT
DIVISION

B-206582

The Honorable J. Charles Partee
Chairman, Federal Financial
Institutions Examination Council

Dear Mr. Partee:

This report discusses the adequacy of information on the ancillary activities of the Nation's banks, savings and loan associations, and their related holding companies and on commercial firms' growing involvement in traditional banking activities. U.S. banking policy and regulations have long maintained a separation of banking and commerce. In recent years, however, a number of changes have blurred the distinctions between banking and commerce and have fostered an industry structure quite different from what has previously existed.

Nonbanking companies are rapidly expanding the range and volume of financial services they offer and are becoming more and more like banks. Savings and loan associations are becoming more banklike, are breaking down traditional geographic boundaries, and are more easily affiliated with commercial enterprises. Banking firms are responding to this challenge of increased competition in their traditional markets with innovative expansions of their own. While reactions to these changes are predictably mixed, there is increasing pressure to do away with the regulations that have kept banking and commerce separate. For example, S. 1720, among other things, proposes to (1) expand the investment-banking-like powers of commercial banks, (2) expand the commercial-banking-like powers of savings and loan associations, (3) facilitate the cross-ownership of banks and savings and loans, and (4) reduce the geographic barriers to depository institution expansion.

The Congress and the financial institution regulators are being asked, in effect, to decide if the national policy of separating banking and commerce is still appropriate. Such a decision should consider whether currently permissible activities are having an adverse impact on the depository institutions' safety and soundness and whether the merging of banking and commerce is helping promote the economic and public benefits of the financial service industry. However, the information needed to illuminate these issues is not readily available to the financial institution regulators. Some information on ancillary activities of the depository institutions and nonbanking activities of the holding companies is available, but often it is inaccurate or misleading. In addition, some needed information is not collected or not compiled in a manner to facilitate analysis. We believe that information about ancillary activities needed by policy makers and regulators should be gathered in a manner consistent with the intent of the Paperwork Reduction Act of 1980.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this review was to compile information on the activities of the major depository institutions and their related holding companies and the banklike activities of commercial firms to determine their nature, scope, and significance. This information was then analyzed to develop an understanding of the merging of banking and commerce and to determine if adequate data was available for the Congress and the Federal bank regulators to be informed about the changing financial services industry. The review was conducted in accordance with GAO's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions."

In compiling information on the ancillary activities conducted by banks and savings and loan associations, we focused on those activities conducted by separate subsidiary companies. While depository institutions can conduct some ancillary activities directly, rather than through subsidiaries, we did not attempt to study these internal activities as information on them is generally not available.

Our primary source of information on the activities of the depository institutions was the data submitted by them to the Federal regulators. In some cases, the available data were inaccurate or incomplete. We therefore supplemented these data with data from the agencies' examination reports and the institutions' financial statements.

Although in some cases more current data were available at the time of our review, 1979 was selected as the period for our analysis because data for that period were more complete and thus better assured comparability among the various sources of information.

A number of sources were used in compiling information on the ancillary activities of the depository institutions.

--For banks and nonbanking subsidiaries associated with bank holding companies, we used the computerized data compiled on the Federal Reserve Board's bank holding company data base.

--For banks not associated with bank holding companies, and for overall bank statistics, we relied on the "Call Report." These data are provided by the banks to their appropriate Federal regulatory agency.

--For information on the nature and extent of banks' ancillary activities, we relied on two sources.

1. For publicly held banks reporting subsidiaries, we reviewed the annual reports filed in accordance with the Securities Exchange Act of 1934.

2. For the remaining banks reporting subsidiaries, we used the regulators' examination reports.

--For subsidiary activities of savings and loan associations, we relied on the computer data compiled from two reports.

1. The Semiannual Financial Report and

2. The Financial Report for Wholly Owned Service Corporations.

--For the activities of the savings and loan holding companies and multi-owned service corporations, we reviewed and compiled information that is based on data they submitted to the Federal Home Loan Bank Board.

We conducted a reliability assessment of the Federal regulators' computerized data to determine if the information reported by the depository institutions was accurately compiled. This assessment was not designed to evaluate the entire data base of each of the agencies, but rather to see if some of the key data elements used in our analyses were accurately compiled. This assessment indicated the data used were compiled as reported; however, as we will later discuss, we found a number of errors and deficiencies in the Federal regulators' data.

Information on the nature and extent of banklike activities of commercial firms was taken from a number of studies, articles, financial reports, and data provided by various trade associations. In addition, we used information submitted to the Securities and

Exchange Commission (SEC) in accordance with the Securities Exchange Act of 1934.

BANKING AND COMMERCE TRADITIONALLY SEPARATED

National policy and congressional intent have traditionally held that banking be separate from commerce. This separation was based on the belief that the merging of banking and commerce could undermine the safety and soundness of these institutions. Another concern has been that the intermingling of these activities could unduly concentrate resources and ultimately diminish competition, thereby undermining our economic system.

Over the years various regulations have dealt with the subject of separating banking from commerce.

- --The authority for national banks to conduct ancillary activities dates from the National Bank Acts of 1863 and 1864. Originally only a few "nonbanking" powers were authorized, and the acts specifically forbade national banks from operating or investing in commercial or industrial ventures. Over the years a number of additional activities have been authorized as "incidental powers."

- --The Banking Act of 1933 (popularly known as the "Glass-Steagall Act") further defined the barrier between banking and commerce. Banks were not allowed to engage in investment banking. Investment banking was essentially defined as issuing, selling, underwriting, and/or distributing securities. With some exceptions for certain types of Government securities, commercial banks were not allowed to engage, directly or indirectly, in such activities.

- --The basic legislation covering holding company activities dates from the Bank Holding Company Act of 1956. This act was amended in 1966, 1970, and 1978. As it currently exists, organizations which own or control a bank are permitted to engage only in activities closely related to banking.

- --Investment by Federal savings and loan associations in ancillary activities, called service corporations, is authorized by the Home Owners' Loan Act of 1933. This act was amended in 1964. In 1980, the Depository Institutions Deregulation and Monetary Control Act expanded the amount of investment an association may have in a service corporation from 1 to 3 percent of assets.

--The Spence Act (section 408 of the National Housing Act), enacted in 1959, represented the first regulation dealing with holding company ownership of savings and loan associations. In 1967, the Savings and Loan Holding Company Act Amendments were passed to strengthen the legislation in this area.

SEPARATION OF BANKING AND COMMERCE IS BECOMING LESS DISTINCT

Although the separation of banking and commerce has been a fundamental concept of our banking system, the structure and functions of the financial service industry have been so altered in recent years that it is becoming increasingly difficult to tell the difference between the two. Today, banks, savings and loan associations, and their related holding companies engage in a number of activities (and on a scope) that in years past would have been thought to be far removed from the normal business of banking. At the same time, nonbanking firms are providing financial services traditionally considered as part of banking.

Ancillary and nonbanking activities of depository institutions and their related holding companies

Banks and savings and loan associations conduct a wide range of ancillary activities which are outside the scope of their deposit and lending activities. In 1979, 927 of the 14,364 federally insured banks and 1,970 of the 4,039 insured savings and loan associations reported owning or controlling subsidiaries. The majority of the bank subsidiaries operated for the purpose of holding the banks' premises, and the most frequent savings and loan association subsidiary activity was for real estate development and sales. Banks and associations were also involved in such activities as mortgage banking, leasing, and insurance.

Bank holding companies and savings and loan holding companies frequently engage in nonbanking activities. Bank holding company nonbanking activities are similar to those conducted by banks; however, they are considerably more extensive. In 1979, about 630 bank holding companies reported owning subsidiaries other than those associated with their banks; and, while most bank holding companies have no nonbanking subsidiaries, some have dozens, even hundreds, of them.

Savings and loan holding companies may conduct many of the same activities permitted savings and loan associations; however, in contrast to the limited activities authorized for bank holding companies, savings and loan holding companies owning only one savings and loan association are not restricted in the types of businesses they may conduct. Consequently, the primary business of some is far removed from banking, and a number of these companies have dozens of subsidiaries conducting a wide range of activities including manufacturing, entertainment and broadcasting, and mining.

Many commercial firms
provide financial services

Commercial firms have captured a significant share of today's financial services market and are continuing to actively expand their market shares through provision of more and more banklike services. The following examples, which are by no means inclusive, illustrate how far firms have gone in reshaping the financial services industry.

--Total assets held in money market mutual funds reportedly grew in 1981 from $77 billion to over $180 billion.

--In addition to accepting consumer deposits, some money market funds offer checking services.

--Several major retail and industrial firms have entered the consumer banking business by acquiring savings and loan associations or by acquiring existing commercial banks and divesting them of their commercial loan portfolios.

--One of the Nation's largest insurance companies has acquired a major brokerage firm which also operates large money market mutual funds.

Depository institutions are attempting to
expand the types of products they can offer

Commercial banks and savings and loan associations, although more closely regulated than commercial firms, are exploring and finding new ways to broaden the financial services they can offer to answer the challenge of their competitors. Some recent examples include:

--Several large banks and savings and loan associations are reportedly studying ways to acquire security brokerage firms, while others have already announced such acquisitions pending regulatory approval.

--One bank has applied to its regulator for permission to create the banking institution's first financial futures brokerage firm.

--Several banks and savings and loan associations have announced plans to establish money market mutual funds.

ARE ANCILLARY AND NONBANKING ACTIVITIES SAFE?

Some of our previous reports have indicated that ancillary activities may adversely affect the safety and soundness of the depository institutions and their related holding companies. In 1978, we reported that the subsidiaries of savings and loan associations were increasingly being cited as contributing to the associations' problems. 1/ We noted that while only 40 percent of the federally insured associations owned subsidiaries, 68 percent of the identified problem associations had subsidiaries. Similarly, our 1981 report on the efficiency of bank holding company inspections noted that bank holding companies with nonbank subsidiaries had a higher incidence of problems than companies without subsidiaries. 2/

Overall, about 16 percent of the holding companies with nonbanking subsidiaries were experiencing problems while only about 6 percent of the companies without nonbank subsidiaries were experiencing problems. Holding company inspectors told us that nonbank subsidiaries, especially credit-extending ones, present a significant holding company risk. One Federal Reserve Board official said that even a small nonbank subsidiary may pose a threat to the holding company. For example, in one instance the nonbank activity made up less than one-tenth of 1 percent of the holding company's assets; however, when the subsidiary experienced a heavy loss, it resulted in cash flow problems for the holding company. The holding company's earnings were used to cover the subsidiary's losses, thus weakening the overall financial position of the holding company and its bank and nonbank subsidiaries.

1/"Savings and Loan Associations: Change Needed in the Regulation of Their Service Corporations" (FOD-78-4, June 14, 1978).

2/"Federal Reserve Could Improve the Efficiency of Bank Holding Company Inspections" (GGD-81-79, Aug. 18, 1981).

INFORMATION ON ANCILLARY ACTIVITIES AND THE BANKLIKE ACTIVITIES OF COMMERCIAL FIRMS IS INADEQUATE

Future deliberations concerning the reasonableness of the existing regulations and the merits of either tightening or relaxing the general prohibition against merging banking and commerce could be greatly enhanced by knowing if

--the currently permissible ancillary and nonbanking activities have adversely impacted on safety and soundness, and

--the merging of banking and commerce is having an adverse impact on competition and is creating an undue concentration of financial resources.

However, adequate data to evaluate the impact of ancillary and nonbanking activities and the merging of banking and commerce are not readily available to Federal policy makers and regulatory officials.

Lack of data on ancillary and nonbanking activities

The banking regulators currently require depository institutions and holding companies to report their activities and the results of their operations. However, as discussed below, these reports do not provide adequate information on the nature and scope of their activities.

Call report

All federally insured U.S. banks submit information on their financial condition and results of operation by means of a so-called "Call Report." This report serves as the basic information-gathering tool for statistical and operational data.

This report, however, is deficient in providing information on ancillary activities because the banks are only required to report the number of major subsidiaries they control, if any, and even this limited information appears to be unreliable. The banks do not identify the nature of business engaged in by their subsidiaries nor any financial information about the subsidiaries' operations. In addition, our verification of the Call Report, comparing it with regulators' examination reports and/or statements submitted to the SEC, shows that for 100 of 462 banks, subsidiary data may have been reported inconsistently. Thirty-one banks incorrectly reported the number of subsidiaries they operated. In one case, a bank reported 85 subsidiaries, when in fact it had none. 1/ Also, 69 banks reported that they operated subsidiaries although we found no mention of subsidiaries in the examiners' reports or statements filed in accordance with the SEC requirements.

Bank holding company data base

Information on bank holding companies is reported to the Federal Reserve Board by means of a number of different reports and compiled on the bank holding company data base for research, statistical, and supervisory purposes. However, financial information is available for only a minor portion of the bank holding companies. For 1981, only about 775 of the approximately 3,640 holding companies will have their financial information compiled on this data base. The remaining holding companies are not required to file financial statements in a form which lends itself to computerization. In response to our recent report which addressed this subject, the Federal Reserve Board told us that it plans to computerize the financial data.

Not only is the information compiled on the bank holding company data base limited, it is often difficult to use for analysis purposes. Problems we noted include the following:

--The financial and structural information on the companies is frequently duplicated because of the tiered ownership of some holding companies.

--The type of business conducted by many subsidiaries is not shown.

--Often the information needed to distinguish whether a subsidiary is operated by a bank or directly by the holding company is not indicated.

--Financial information on all the ancillary activities of banks and many nonbanking activities is not available.

Savings and loan data base

Information on the ancillary activities of savings and loan associations is more complete than that available on the activities conducted by banks and their holding companies. For example,

---

1/The bank had reported that each of its branches was a subsidiary.

the associations report their investment in and income from their ancillary activities; banks do not. Also, each service corporation which is owned by a single association is required to provide information on its financial condition and the type of business it conducts. In addition to being more complete than the information furnished by banks and their holding companies, the data are computerized in a form that facilitates analysis.

Nevertheless, there are two aspects of the savings and loan industry for which data are not routinely compiled:

--the nature and scope of the ancillary activities of service corporations owned by more than one association and

--information on the holding companies that own associations.

Federal Home Loan Bank Board officials told us they do not routinely compile information on these aspects of the savings and loan industry because the influence of these activities on the institutions is relatively minor. At the end of 1979, there were only 76 service corporations with assets of $165 million owned by more than one association as compared to 2,447 wholly owned service corporations having assets of $4.8 billion. At the same time, there were only 98 savings and loan holding companies owning 133 of the 4,039 federally insured savings and loans.

Lack of data on the banklike activities of commercial firms

In contrast to the rather stringent reporting requirements imposed on depository institutions, commercial firms conducting banklike activities generally do not report their activities in a form that can be readily compiled and analyzed. Commercial firms submit information for income tax purposes and to adhere to various regulatory requirements, such as the Securities Exchange Act of 1934 which pertains to publicly held companies. However, while general statistics on major industries are compiled, the available data do not show the nature and extent of banklike activities conducted by commercial firms. For example, often firms filing statements in accordance with the Securities Exchange Act of 1934 may be engaged in banklike activities or businesses similar to those conducted by depository institutions. However, financial information on these activities is not shown, instead results of these operations are consolidated with data on other operations in the firms' overall financial statements.

CONCLUSIONS

Since it was first established, the national policy separating banking and commerce has been refined and revised. However, recent actions by all participants in what is now being called the financial services industry have focused attention on this policy. The regulators and the Congress are being asked to modify if not eliminate the policy. The policy grew from concerns about banking safety and soundness and the concentration of financial power--concerns which policy decisionmakers address today as well. Yet, we believe that the information needed to address these issues is not readily available.

The various banking regulators' reporting systems do not adequately disclose the nature and extent of depository institutions' and holding companies' involvement in ancillary and nonbanking activities. In addition, adequate information does not exist on the banklike activities conducted by commercial firms. As a consequence, the regulators and the Congress do not have information needed to assess the impact of these activities and to formulate appropriate policies, legislation, and regulations directed at the merging of banking and commerce and the financial services industry as a whole. Before reaching any conclusions regarding these issues, the regulators and the Congress should be fully aware of just how closely banking and commerce are already aligned and how current and future relationships could affect safety and soundness and financial concentration. Therefore, we believe that the regulators, acting through the Federal Financial Institutions Examination Council, should act to improve the extent and accuracy of information on the ancillary operations of banks, savings and loan associations, and their holding companies.

We recognize the need to reduce, to the extent possible, the reporting burden placed on private entities by only collecting information that (1) is necessary, (2) is not duplicative, and (3) can be used. In fact, these are the mandates set down in the Paperwork Reduction Act of 1980. However, we believe that complete and adequate information about the extent and nature of nonbanking activities of depository institutions is needed by the Congress and the regulatory agencies to meet their policymaking and regulatory responsibilities. This information is not readily available to these institutions and should be collected, considering the rapidly changing nature of the financial industry. Consequently, collecting the needed information is consistent with paperwork reduction objectives of the Paperwork Act.

RECOMMENDATION TO THE FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

We recommend that the Federal Financial Institutions Examination Council identify the needs for information about ancillary activities and design, test, and implement a collection instrument that would efficiently capture only the minimal amount of information that is necessary and useful, thus minimizing respondents' paperwork burdens.

AGENCY COMMENTS AND OUR EVALUATION

A draft version of this report was furnished to the Federal Financial Institutions Examination Council, the Board of Governors of the Federal Reserve System, the Federal Home Loan Bank Board, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation for their review and comment. The Federal Reserve Board and the Federal Home Loan Bank Board did not comment. The other agencies' comments are reproduced in appendixes I, II, and III.

The Comptroller (see app. III) said that one problem in collecting information on ancillary activities is that activities that were once considered "nonbanking" are now commonly considered to be part of "banking." Because we agree that the distinctions between banking and nonbanking have become less clear, we believe that better information on ancillary activities is needed.

The Comptroller also said that (1) mandatory reporting for the purpose of evaluating the impact of ancillary activities is not necessary, and (2) separate reporting of subsidiaries, beyond what is now reported on a consolidated basis in Call Reports, is also unnecessary. Yet, the Comptroller points out that a major objective of his organization's "Strategic Plan for the 80's" is to identify and monitor changes in the financial system. He also recognizes that reporting requirements must provide sufficient information to enable his organization to determine the relative strengths and weaknesses of subsidiary companies. We agree with this objective and believe that it supports our conclusion that better information on ancillary activities is worthwhile.

Both the Council (see app. I) and the Corporation (see app. II) contend that a new and expanded reporting system is not warranted at this time. Rather, they believe that improvements in their information collection capabilities can be made with little or no additional burden being imposed on financial institutions. They explain that, currently, a number of efforts are underway to identify whether data is needed and how it can be collected.

We agree that a new system is not necessary, and did not recommend that one be created. We believe that needed information could be obtained by augmenting currently required reports and increasing the use of examination and inspection procedures.

- - - -

Section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report.

Copies of this report are being sent to the Chairmen of the Senate Committee on Governmental Affairs; the House Committee on Government Operations; the Senate Committee on Banking, Housing and Urban Affairs; and the House Committee on Banking, Finance and Urban Affairs. Copies are also being sent to each of the Federal depository institution regulators.

Sincerely yours,

W.J. Anderson

William J. Anderson
Director

Federal Financial Institutions **Examination Council**, Washington, D.C. 20219

April 21, 1982

Mr. William J. Anderson
Director
United States General
Accounting Office
Washington, DC 20548

Dear Mr. Anderson:

On behalf of the Examination Council, I am pleased to respond to your letter of March 24, 1982, requesting comments on the General Accounting Office's draft report entitled "Information About Depository Institutions' Ancillary Activities Is Not Adequate For Policy Purposes." After careful study of the report, the Examination Council has come to the conclusion that the creation of a new and expanded reporting system dealing with depository institutions' ancillary activities is not warranted at this time.

The GAO study suggests that, in order for Congress to determine whether and to what degree the merging of the fields of commerce and banking should be permitted, more complete and accurate information is needed about the extent to which ancillary activities of banking and nonbanking firms are crossing the traditional boundaries of these two broad lines of activity. The GAO also indicates that the information being collected on depository institutions and their holding companies is not sufficient to assist policymakers and regulators in evaluating the effect of such ancillary activities on competition and on the financial condition of depository institutions.

As you know, commercial banks and their parent companies are prevented by statute and regulation from engaging in activities other than those that are closely related to banking. The same holds true for savings and loan association holding companies that control more than one association. The ancillary activities of these types of institutions are well known to their respective regulators through their current approval and reporting mechanisms and from information gathered on-site by agency examiners. Although single savings and loan association holding companies may engage in "nonbanking" activities, those that actually do so are few in number and their commercial activities are well known to the regulators.

It seems to us, instead, that the breech of the once largely distinct fields of commerce and banking is occurring almost entirely from the other side - namely, the expansion of nonbanking enterprises into activities long regarded as banking oriented. As noted, it does not appear that depository institutions are expanding into areas that have been historically in the realm of commerce, due to the legal restrictions.

While the Council does not believe that substantial new reports are warranted for the purpose of identifying the ancillary activities of holding companies, banks and savings and loan associations, it may be that some additional

Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Federal Home Loan Bank Board
National Credit Union Administration, Office of the Comptroller of the Currency

Mr. Anderson - 2 -

information could be useful. The Council believes, however, that such additional information probably could be garnered through the normal examination process conducted by the regulators. If so, little or no additional burden would be imposed upon the financial institutions. Although this approach means that the information would not be for the same point in time, the nature of the gaps that exist is such that the time element is not regarded as critical.

In response to GAO's recommendations, therefore, the Council has assigned to its Task Force on Supervision the responsibility for assessing what types of additional data may be needed and whether such information can be collected through the normal examination or inspection procedure. In addition to evaluating the information currently available in the various supervisory reports,the Task Force will make a determination as to how these data might be supplemented.

Also to be included as a part of the review will be a study of current information-gathering procedures and whether they need to be altered. Once the Task Force has reached its conclusions, the Examination Council will review those findings and determine what, if any, recommendations it wishes to make to the agencies for collection of additional data through the examination process.

The Council believes that the effects of holding company and subsidiary operations on the safety and soundness of depository institutions are currently being subjected to careful and thorough review by the agencies. Although the regulators during the normal course of the on-site examination process look into all activities of holding companies, particular scrutiny is given those areas that could affect the financial strength of the parent or other affiliates. Any potential or existing problems are brought to the immediate attention of the organization concerned and appropriate supervisory action is then taken.

We appreciate having the opportunity to comment on the GAO's draft report.

Sincerely,

Robert J. Lawrence
Executive Secretary

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, D.C. 20429

OFFICE OF DIRECTOR · DIVISION OF BANK SUPERVISION

April 29, 1982

Mr. William A. Anderson
Director
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson:

Chairman Isaac has asked me to comment on the GAO draft report entitled "Information About Depository Institutions' Ancillary Activities is Not Adequate for Policy Purposes." Although the report discusses the information collection methods of several Federal agencies, our comments are limited to those areas directly related to the FDIC.

The GAO suggests that Congress and the financial institution regulators are being asked to evaluate deregulation proposals that modify the "national policy separating banking and commerce" without adequate data either on nonbank activities of depository institutions or on commercial firms that conduct banklike activities. While we agree that analysis of a complex issue is made easier with detailed and accurate research data, we question the practicality of GAO's proposal for a new information collection system.

Before such a proposal can be considered, a number of important issues need to be addressed. Paramount among them is the cost to the regulatory agencies and to the financial industry relative to the value of the data. We believe the staff time required to design, test, coordinate, collect and review this data would be substantial. Also, it is unclear whether data collected from a diverse universe of financial entities could be grouped into a meaningful format. Moreover, we doubt that such a major project could be cost justified under the Paperwork Reduction Act. The Office of Management and Budget has requested all Federal agencies to reduce public burden by a 25 percent total over fiscal years 1982 and 1983. If such goals are to be achieved, the gathering of new information must be offset by the deletion of already constricted information, and further constriction could adversely impact our monitoring capability to unacceptable levels.

It should be noted that ancillary and nonbank activities, although increasing, remain small in relation to overall bank business. In our judgment sufficient monitoring techniques are already available. Examiners routinely review the financial data of a bank subsidiary and closely monitor intercompany transactions. When appropriate, a detailed review of the subsidiary's internal operation is performed. Similarly, holding company activities are subject to detailed inspections by the Federal Reserve System's holding company examiners.

We are not opposed to improving our information collection capabilities. However, instead of developing a new information collection system as proposed by the GAO, it may be more cost-effective to improve the efficiency and accuracy of systems already in place. Toward this end, the Federal regulatory agencies have taken positive steps. Recently, a task force on holding company supervision was established with representatives from FDIC, the Office of the Comptroller of the Currency, the Federal Reserve Board and the Federal Home Loan Bank Board. The objectives of this task force include the development of a coordinated examination program for holding companies and improvement of current information collection systems for all holding company activities.

A second task force is reaching the final stages of devising a substantially improved Report of Condition and Report of Income. These reports are the major source of bank data provided by the banking industry, and completion of this project will significantly improve our information collection and monitoring capabilities in all areas of banking.

In summary, while some deficiencies exist in our present information collection systems, they can be minimized through continued cooperative efforts with the other Federal regulators. We appreciate the opportunity to comment on this report and would be willing to elaborate on any of these comments with you or your staff.

Sincerely,

Quinton Thompson

Quinton Thompson
Director

Comptroller of the Currency
Administrator of National Banks

Washington, D.C. 20219

May 5, 1982

Mr. William J. Anderson
Director
General Government Division
U.S. General Accounting Division
Washington, D.C. 20548

Dear Mr. Anderson:

We appreciate the opportunity to respond to GAO's draft report entitled "Information About Depository Institutions' Ancillary Activities Is Not Adequate For Policy Purposes." GAO recommends that additional information is needed on nonbanking activities of depository institutions to assist in making policy decisions. The report directs the Federal Financial Institutions Examination Council (FFIEC) to assume the lead role in designing, testing and implementing a collection instrument to gather the necessary data. The Office of the Comptroller of the Currency (OCC) offers the following comments for GAO's consideration.

A major problem with the thrust of the GAO draft report is the inherent difficulty of defining "banking" and "nonbanking". The business of banking is not solely limited to deposit and loan functions as the report implies. Rather, the business of banking includes many activities which the GAO might denote as ancillary or auxillary activities. One example of this is leasing which in the past may have been thought of as a nonbanking activity but now is merely another form of financing in the banking community. The rapid advancement of technology contributes to the almost impossible task of precisely defining "banking" and "nonbanking" activities.

This major problem also will affect the ability of the FFIEC to collect any data, since each financial regulatory agency may have its own definition as to what is or is not a "banking" activity. Since the orientations of the regulated financial institutions vary from agency to agency, it may be impossible to reach a consensus on what type of data are necessary to focus on this issue.

Mr. William J. Anderson
Page 2

We agree that the report accurately describes the limited data available on ancillary activities of both bank subsidiaries and holding companies. It should be noted though, that we do not advocate increasing the reporting burden on the depository institutions just for the sake of collecting data. Identification of the significant policy matters for decision-making purposes must be made before determination of data requirements takes place. It is the OCC's position that mandatory reporting for purposes of evaluating the impact of ancillary activities on banks' and their operating subsidiaries' performance is unnecessary, however, additional data on holding companies might be helpful, since their scope of activities tends to be broader.

The OCC views banking institutions on a consolidated basis, emphasizing the close interrelationship between parent bank and subsidiaries. In most cases a bank conducts ancillary activities as a separate department of the bank with bank personnel serving dual capacities. In the draft report GAO correctly points out that the vast majority of bank subsidiaries are established merely to hold bank premises. For that reason, we submit that it becomes unnecessary to require separate or additional financial reporting requirements for bank subsidiaries. Existing call reports consolidate the activities of significant majority owned subsidiaries so that the performance of the entire organization can be determined.

Additional information on ancillary activities of holding companies might be useful since these activities tend to have a broader range than bank subsidiaries. At present, only summary information is collected on bank holding companies through the Federal Reserve Board. Data on the activities of both nonbanking companies and consolidated financial reports are not available. Presently it is not possible to estimate the impact of interest rate changes on a multi-subsidiary holding company. Annual report information may be used on an individual case basis, however, SEC reporting requirements do not collect the proper data to make comparative analyses.

As addressed in the OCC's Strategic Plan for the 80's, one of our major objectives is to maintain the capability to identify and monitor changes in the financial system. This will require reallocating our resources and improving or refining our supervisory techniques. Therefore, it is important that the reporting requirements provide sufficient data to enable us to determine the relative strengths and weaknesses of subsidiary companies. The information obtained should enable analyses and detection of problem areas. Once detected, these areas then would be further investigated. It is anticipated that as we obtain pertinent remote or off-site information we will limit the scope of our on-site examinations and thus follow our long range planning philosophy.

Mr. William J. Anderson
Page 3

A final issue that should be further addressed by GAO concerns the reporting burden imposed on depository institutions. The FFIEC will have to analyze from a cost/benefit basis the utility of the additional data required. They will have to focus on whether this reporting requirement will be a handicap to the competitive process since other "nonbanking" institutions will not have this additional responsibility. Finally, it must be decided if the added burden is consistent with the objective of attaining a level playing field for all providers of financial services. The answers to these items may provide the framework for completely addressing GAO's recommendation.

Sincerely,

C. T. Conover

C. T. Conover
Comptroller of the Currency

(233057)

21996

AN EQUAL OPPORTUNITY EMPLOYER

UNITED STATES
GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

OFFICIAL BUSINESS
PENALTY FOR PRIVATE USE, $300

POSTAGE AND FEES PAID
U. S. GENERAL ACCOUNTING OFFICE

U.S. MAIL

THIRD CLASS