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Manager
Dissemination Branch
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Midland Financial Co. and MidFirst Bank ("MidFirst") appreciate the opportunity to comment on the Office of Thrift Supervision's (OTS) proposal to establish regulation requiring Savings and Loan Holding Companies to notify the OTS of significant new transactions or activities as well as proposals to establish minimum capital requirements on savings and loan holding companies. MidFirst requests the OTS to reconsider the proposed rule for the following reasons:

- MidFirst does not believe federal statute, particularly the Home Owner's Loan Act ("HOLA"), or Congressional intent provides the OTS with the authority to require prior notification for new activities of savings and loan holding companies.
- MidFirst believes the proposal as written jeopardizes competition.
- MidFirst believes the potential regulatory burden would exceed any potential benefit.

MidFirst agrees with OTS that regulatory oversight of savings associations is prudent to preserve the safety and soundness of the industry; however, the proposed rule is not the appropriate method. MidFirst encourages the OTS to withdraw the proposal. The following elaborates on MidFirst's positions and responds to specific questions raised by OTS in the NPR.

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OTS Authority

Congress provided OTS with the authority to regulate savings associations; however, Congress never intended for the types of actions as proposed by OTS to extend to the savings and loan holding company level. As the OTS notes in the Notice of Proposed Rulemaking ("NPR"), the OTS has statutory authority pursuant to 10(g)(5) and 10(p) of HOLA to take action on a remedial basis in response to holding company actions which the Regional Director concludes has a "reasonable cause to believe that the continuation . . . constitutes a serious risk to . . . subsidiary savings association"; however, there is no similar authority for the actions proposed in the NPR. Of particular note is that OTS did not cite any express statutory provision that authorizes the agency to require savings and loan holding companies to notify OTS before engaging in certain activities as outlined in the NPR. The NPR proposes to expand OTS oversight of activities *proposed by* a savings and loan holding company whereas 10(g)(5) addresses existing activities and 10(p) addresses acquisition of a savings association.

Review of the *Congressional Record* of November 3, 1999, and November 4, 1999, reveals discussion of the unitary thrift holding company provision contained in Gramm-Leach-Bliley.

- Comments made by Senator Johnson and noted on page S13875 of the Congressional Record succinctly express the intent of Congress regarding this provision: "The conference report does not interfere with current ownership of thrifts. Any commercial firms that currently own a unitary thrift charter will be able to continue to own and operate their institutions *without restriction*. Their current status would be undisturbed. The only limitation this amendment would impose involves the transferability of that charter." Senator Johnson continues: "Only the current, limited universe of legitimate unitaries should be allowed to exercise powers granted them in the Home Owners Loan Act . . ." (emphasis added).

- Senator Kerry expresses similar sentiment on page S13904: "Under the conference report, current unitary thrift holding companies and their savings association subsidiaries would be able to continue their normal activities."

- Senator Gorton's comments on page S13906 include: "Neither the FDIC or the primary federal regulator have identified any safety and soundness concerns during the three decade existence of unitary thrifts. Not one."

- Similar Congressional intent is documented beginning on page H11513 of the November 4, 1999, *Congressional Record* memorializing debate in the U.S. House of Representatives.

The Act's Statement of Managers of the Conference Committee dated November 1, 1999, states that "A grandfathered unitary thrift holding company (one in existence or applied for on May 4, 1999) retains its authority to engage in nonfinancial activities."

Gramm-Leach-Bliley was a comprehensive and much debated regulatory scheme that included the unitary thrift holding company issue. This scheme included no provision for the rule proposed in the NPR. On Page S13914 of the Congressional Record Senator Sarbanes, in discussing S.900, states that: "It is preferable to have a framework developed by Congress, not on an ad hoc basis by one regulator or another regulator . . . If we can have a responsible statutory framework established by the Congress which is contained in this legislation that is now before us, it will contribute to the safety and soundness of the financial system. This legislation better enables us to maintain the separation of banking and commerce." It is clear from Senator Sarbanes' comment that had Congressional intent been to require regulatory oversight of the nature contained in the NPR, that specific statutory authority is the preferred precursor to such regulatory provisions; since Congress did not establish provisions as outlined in the NPR, it can only be concluded that Congress had no such intent.

In short, it is clear that no statutory authority exists to support the requirements in the proposed NPR; it is equally clear that Congressional intent during debate and passage of Gramm-Leach-Bliley was not to provide any authority to limit the operations of grandfathered unitary thrift holding companies. The OTS indirectly acknowledges this by <u>not</u> providing a statutory citation establishing OTS's authority to impose the prior notice requirements on savings and loan holding companies.

MidFirst also notes that in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Public Law 101-73, or FIRREA, Congress explicitly repealed the statutory provision requiring nondiversified savings and loan holding companies to receive approval from the OTS prior to incurring debt that exceeded 15 percent of net worth. The OTS's current proposal in the NPR undermines the specific Congressional action that removed the prior approval requirement.

Finally, the NPR references the Federal Reserve's authority in regard to bank holding companies in an attempt to justify the OTS proposal. MidFirst opines that any such authority allowed the Federal Reserve, as well as the specific oversight that the Federal Reserve imposes on bank holding companies, is irrelevant to the question of the OTS's statutory authority to propose the rule contained in the NPR. Since bank holding companies and savings and loan holding companies are subject to separate and very

different statutory schemes, the Federal Reserve's role and oversight has no bearing on the authorities that Congress specifically granted or intended to grant to OTS in its role of regulating savings and loan holding companies.

Existing Regulation

MidFirst opines that existing regulations offer a reasonable means to discourage and limit abuse of insured savings association subsidiaries by parent holding companies. While it may be true that a misguided decision by holding company management might be difficult to reverse after implementation, OTS is not precluded from taking prudent regulatory action. In fact, OTS has specific and direct authority in relation to the activities engaged in by a savings association and as a result can limit the savings association's activities with the parent.

Less burdensome regulatory mechanisms that limit the savings and loan holding company's interactions with and influence on the insured subsidiary currently exist. Specifically, OTS Transaction with Affiliate regulations at 12 CFR 563.41 and 563.42, Loans to One Borrower regulation at 12 CFR 563.93 as well as other regulations such as Conflicts of Interest at 12 CFR 563.200 and Corporate Opportunity at 563.201 offer adequate regulatory authority for the OTS to limit activities between the insured subsidiary and the parent holding company. Other relevant regulations including the Capital Distribution regulations beginning at 12 CFR 563.140 and the Financial Policies regulation at 12 CFR 563.161 further a) restrict the actions an insured subsidiary can take in response to undue pressure from a parent savings and loan holding company and b) provide OTS with a means of preventing an insured savings association from engaging in harmful activities in response to pressure from the parent savings and loan holding company. Finally, and as noted in the OTS Historical Framework for Regulation of Activities of Unitary Savings and Loan Holding Companies, "The Director may . . . restrict any activity of the thrift that might create a serious risk that the liabilities of the holding company and its other affiliates may be imposed on the thrift. The Director also may order termination of the affiliate's activity or divestiture of the affiliate, after notice and opportunity for hearing."

In testimony before the Committee on Banking, Housing, and Urban Affairs of the United States Senate on June 25, 1998, and February 24, 1999, Director Seidman elaborated on the OTS's ability to limit undue negative influence by the holding company on the savings association subsidiary. Director Seidman stated during the June 1998 testimony that "Both Congress and the OTS have imposed a variety of requirements on unitary (and multiple) SLHCs [savings and loan holding companies] that are designed to protect the safety and soundness of the subsidiary thrift and enable the thrift to perform its core functions and to significantly restrict interactions between the thrift and its parent

holding company and affiliates." Director Seidman concludes the February 1999 testimony by stating:

> "In our experience, the modern thrift charter provides business flexibility and choice coupled with sound regulatory oversight. It permits affiliates of insured depository institutions with insurance, securities, and other firms, but with built-in safeguards to avoid undue risks to the taxpayer and to meet the needs of consumers and communities. Based on our experience, there is no evidence that shows that affiliates permitted in the unitary thrift holding company structure are inherently risky and should be constrained."

Finally, thrifts and holding companies are currently subject to quarterly reporting requirements through the Thrift Financial Report and H(b)-11 which are designed to assist the OTS in identifying material changes in financial condition and activities that are of interest to the OTS. The recently finalized TFR reporting instructions expand reporting requirements to the holding company level. As a result, the OTS will receive information that will identify the types of activities covered by the proposal within 30 days of each quarter end.

Prior Notification

The concept of a prior notification period of 30 days raises serious competitive concerns. Not only will the time period preclude thrift holding companies from acting promptly on opportunities of value and benefit to the holding company, but it also produces the opportunity for those plans to become public knowledge. More troublesome is that the initial 30-day period can be extended so as to make timely action by the holding company more impossible. In short, an opportunity of value may disappear as the holding company notifies the OTS. The proposed regulation therefore is burdensome and anticompetitive.

Attempting to prevent unsafe and unsound actions by regulating activities prior to implementation will result in over-regulation. MidFirst believes that the actual benefit (i.e., ability to predict activities that would cause a serious risk to the insured savings association) of the proposed regulation would not outweigh its burden and potential negative consequences.

While MidFirst opines that the OTS does not have the authority to pursue the rule contained in the NPR, responses to specific questions asked by OTS in the NPR follow.

20 Percent of Asset Exemption

MidFirst acknowledges that a subsidiary thrift that represents less than 20 percent of a consolidated savings and loan holding company assets, a diversified structure, constitutes a small share of a holding company's overall business. However, MidFirst is not convinced that a diversified structure allowing for the 20 percent exemption poses less risk to the subsidiary thrift. MidFirst also considers the 20 percent threshold proposed by OTS to be arbitrary and void of support; no quantifiable basis exists for the 20 percent proposal.

An asset exemption, as well as the capital exemption addressed below, raises a more fundamental question. These exemptions will not only allow for commercial entities that do not own thrifts to have a competitive advantage, but in many cases, unitary thrift holding companies will have a competitive advantage over other unitary thrift holding companies. If the proposed rule is adopted, only those thrift holding companies not meeting an exemption will be forced to delay business decisions pending notification of OTS.

As noted above, the proposal is also contrary to the decision by Congress in 1989 to remove the statutory prior notice regarding increases in debt of nondiversified savings and loan holding companies. As a result, MidFirst is concerned not only with the threshold contained in the NPR, but with the asset exemption in general. More fundamentally, MidFirst believes this proposal is contrary to the statutory authority of HOLA.

Capital Cushion Exemption

Pursuant to 12 CFR 225 Appendix A, bank holding companies must maintain a "minimum ratio of qualifying total capital to weighted risk assets of 8 percent, of which at least 4.0 percentage points should be in the form of Tier 1 capital." MidFirst notes that the NPR proposes a threshold of "consolidated tangible capital of ten percent or greater following the proposed transaction." The disparity between these two standards is significant with the proposed OTS ratio being the more regulatory burdensome. Further, the OTS does not present any basis or justification as to why a ten percent threshold is appropriate or reasonable.

MidFirst opines that the fact that the Federal Reserve has established a capital threshold does not establish a basis for the OTS to impose a capital threshold on savings and loan holding companies. However, the exemption as structured in the NPR would put savings and loan holding companies at a competitive disadvantage in relation to bank holding companies on capital grounds. Congress has never expressed an interest to impose such rules on savings and loan holding companies.

Should the rule exclude de minimus investments and if so what threshold should be established?

In the event that the proposed rule is adopted, a de minimus threshold should be included. The NPR defines consolidated non-thrift liabilities so as to include all liabilities (not just debt obligations) of the holding company and non-thrift subsidiaries. The NPR defines consolidated tangible capital to be tangible capital of the holding company, the non-thrift subsidiaries, and the subsidiary thrift. MidFirst requests clarification of both definitions. If MidFirst's interpretation of consolidated tangible capital is incorrect so that the tangible capital of the thrift should not be included, a de minimus threshold becomes crucial; however, in either case, the 5 percent increase and greater than 50 percent of tangible capital test may produce a significant volume of transactions subject to notification. Not only would OTS be potentially inundated with notices, but holding companies could be precluded from conducting many routine transactions without first filing a notice; for example, once the liability threshold is met, it would appear that the holding company could not purchase even a small amount of office supplies on credit without first notifying the OTS. For holding company structures dominated financially by the assets and liabilities of the thrift subsidiary, this problem becomes more acute.

Since the OTS stated objective is to be made aware of transactions in a more timely manner as opposed to the current method of post-transaction notification via the H(b)-11, MidFirst would suggest that the proposed 12-month activity method be abandoned and a prior quarter activity method be considered. For example, a single transaction occurring early in a 12-month period that triggers the prior notice requirement would result in the need for prior notice on all subsequent transactions, regardless of size. Further, it is reasonable to conclude that once the OTS receives a TFR from an institution, that the OTS is aware of the financial condition of the institution and that material changes in balance sheet structure or size would generate questions by the OTS; as a result, the pertinent test would seem to be for changes in relation to the most recently filed TFR as opposed to a TFR filed six, nine, or twelve months ago. Finally, the 12-month methodology would seem to penalize entities for controlled growth that occurs steadily over several consecutive quarters.

If the OTS proceeds, it should clarify the following and seek public comment before adopting the final rule.

- MidFirst requests specific clarification of the definition of "debt." Does it include formal loan arrangements, commercial paper and bond issuances, accounts payable, accrued salaries, other items?
- Does "debt" mean funds actually drawn or does it include commitments received that have not been drawn?

- Must the increase in consolidated non-thrift liabilities of five percent or more be attributable directly to an increase in debt or is it sufficient for the non-thrift liability growth to be attributable to debt and non-debt factors neither of which individually would trigger the threshold?
- Are both the debt and the consolidated non-thrift liability amounts used in determining the prior notice threshold based on absolute quarter end balances?
- Is the 12-month period used in calculating growth based only on quarter end balances calculated pursuant to TFR reporting? Would this allow intra-quarter growth to exceed the reporting threshold provided the quarter end results were less than the threshold? Would this also allow growth between non-quarter end months (such as between May and October) to exceed the prior notice threshold provided the threshold was not exceeded between March and June, March and September, and March and December?

15 Percent of Asset Threshold

MidFirst requests clarification on the methodology of calculating the 15 percent of asset threshold. Specifically, should the 15 percent be calculated on a) the consolidated total assets of the holding company and subsidiaries but excluding the thrift or b) the consolidated total assets of the holding company and all subsidiaries including the thrift. The NPR implies the latter, but MidFirst requests specific confirmation. If the thrift is excluded from the asset calculation and the thrift dominates the financial structure of the holding company, transactions that are material to the holding company but immaterial to the thrift would be subject to the prior notice requirement; in this scenario, the risk presented to the thrift would be immaterial.

As with the debt threshold, MidFirst requests clarification on how the change in assets is calculated. The NPR states that "the holding company must combine the proposed transaction with all other asset acquisitions conducted during the past 12 months." This presents the opportunity that a series of unrelated acquisitions that fall well below the 15 percent threshold will in aggregate require a prior notice requirement.

MidFirst also requests clarification of the definition of acquisition. MidFirst also asks OTS to review the questions listed in the de minimus section above in relation to asset growth triggers.

Holding Company Capital Requirement

MidFirst opines that there is no statutory basis for the OTS to impose a minimum capital requirement on savings and loan holding companies and requests clarification on this matter. Once clarification is received, MidFirst supports the opportunity for the industry to review and to comment on any proposed capital requirement. MidFirst is specifically

concerned that any proposed capital requirement must not penalize a grandfathered unitary savings and loan holding company for those activities in which it is lawfully engaged. Such a penalty would include higher capital requirements on commercial activities permissible for grandfathered unitaries; imposing such a penalty would be contrary to the statute and history of Congressional intent regarding unitary savings and loan holding company powers. To reiterate Senator Johnson's comments during floor debate of S. 900 on November 4, 1999: "Any commercial firm that currently owns a unitary thrift charter will be able to continue to own and operate their institutions without restriction. Their current status would be undisturbed. The only limitation this amendment would impose involves the transferability of that charter" (*Congressional Record* S13875). While Senator Johnson was not specifically discussing capital requirements of savings and loan holding companies, it is clear that the intent of closing the unitary thrift "loophole" and establishing the grandfather provision was not to impose any new impediments, regardless of form, on grandfathered unitaries.

As mentioned in the "Capital Cushion Exemption" above, bank holding companies have a risk based ratio requirement of eight percent. Should the OTS pursue a capital requirement on savings and loan holding companies, MidFirst does not believe the best interests of the public or the industry would be served by a capital requirement more stringent than that imposed by the Federal Reserve on bank holding companies. While MidFirst reaffirms its position that no statutory basis exists for the OTS to impose capital requirements on savings and loan holding companies, it also notes that any capital requirement exceeding that of bank holding companies would be inequitable.

For the above reasons, MidFirst requests that the Office of Thrift Supervision withdraw the proposed rule.

Sincerely,

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