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Via Facsimile and Airborne Express

February 8, 2001

Manager, Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: Docket No. 2000-91

Re: Proposed Rule Concerning Notice of Significant Transactions

Dear Sir or Madam:

Merrill Lynch & Co., Inc. ("Merrill Lynch") appreciates the opportunity to comment on the rule proposed by the Office of Thrift Supervision ("OTS") on October 27, 2000 concerning notice of significant transactions. Merrill Lynch is a holding company that, through its subsidiaries and affiliates, provides investment, financing, advisory, insurance, and related products and services on a global basis to a wide array of clients. These clients include individual investors, small businesses, corporations, governments and governmental agencies, and financial institutions. By virtue of its ownership of Merrill Lynch Trust Company, FSB, Merrill Lynch is a savings and loan holding company.

The proposed rule would require savings and loan holding companies to provide at least 30 days' prior written notice to OTS before entering into, or committing to enter into, certain debt transactions and asset acquisitions. OTS would have up to 30 days after it deems that it has received all required information before taking action. It could then disapprove or impose conditions on proposed transactions or acquisitions determined to pose a material risk to the financial safety, soundness or stability of a holding company's thrift. The proposed rule would exempt a holding company if its subsidiary thrifts have consolidated assets that, in the aggregate, constitute less than 20 percent of the holding company's consolidated assets or if the holding company would have consolidated tangible capital of at least 10 percent after the proposed transaction or acquisition.

FEB-08-2001 17:32 MERRILL LYNCH 212 670 4503 P.02/07

While we understand OTS's desire to meet the supervisory challenges of a changing financial services industry, we wish to voice our concerns about the proposed rule. We believe that the rule will be burdensome from both a compliance and an administrative standpoint. We further believe that it will unnecessarily intrude upon the ability of a savings and loan holding company and its non-thrift subsidiaries to conduct business in the ordinary course.

Merrill Lynch and its non-thrift subsidiaries engage almost daily in transactions of the type that would be covered by the proposed rule if Merrill Lynch were not otherwise eligible for the proposed exemptions. Our experience does not support the notion that engaging in debt transactions or asset acquisitions of the type addressed by the proposed rule poses an inherent risk to our thrift subsidiary that would justify the proposed intervention in our ordinary commercial activity. We believe that risk to the thrift subsidiaries of a savings and loan holding company should continue to be evaluated consistent with OTS's long-standing precedent – by focusing on the direct impact to the thrift and on transactions between the thrift and its affiliates. We believe that OTS's existing supervisory tools, including limitations on affiliate transactions, dividend restrictions and prompt corrective action powers, are more than adequate to address risks to thrifts within a holding company. Creating a new supervisory scheme would seriously hamper savings and loan holding companies operating in the ordinary course and would interfere with the careful scheme of functional regulation provided by Congress in the Gramm-Leach-Bliley Act. Accordingly, we urge OTS to withdraw the proposed rule. At the very least, OTS should significantly limit the scope of the proposal to address only material debt transactions at the holding company, and to eliminate the coverage of asset acquisitions.

Exemptions

The proposed rule would exempt a holding company whose thrifts have consolidated assets that in the aggregate constitute less than 20 percent of the holding company's consolidated assets. It would also exempt a holding company that would have consolidated tangible capital of at least 10 percent after the proposed transaction.

Notwithstanding these exemptions, an OTS Regional Director would have authority to require the holding company to provide advance notice if the Regional Director has "concerns" about the holding company's financial condition or the safety and soundness of its thrift. The proposal does not set forth any guidelines for making this determination. We are not aware of any precedent for a federal banking regulator to be able to take action based upon such a vague standard.

In several public statements discussing the supervisory challenges facing OTS and explaining the concerns and rationale behind the proposed rule, Director Ellen Seidman has pointed to several large diversified savings and loan holding companies, including Merrill Lynch, as examples of the newer, more diverse holding companies that have

FEB-08-2001 17:32 MERRILL LYNCH 212 670 4503 P.03/07

caused OTS to rethink its supervisory approach.[1] One could infer from these statements that such companies are the targets of the proposed rule despite the exemptions it would provide.

Accordingly, regardless of the present eligibility of Merrill Lynch and other holding companies for the exemptions contained in the current proposal, we are concerned that the overriding authority of the Regional Directors could be used to negate those exemptions. Furthermore, changes in circumstances at savings and loan holding companies or their thrift subsidiaries may reduce the availability of the proposed exemptions without any real change in the potential impact of holding company activities on the thrifts.

Debt Transactions

The proposed rule would require a holding company to notify OTS prior to issuing, renewing or guaranteeing debt that would, taken with all other transactions during the year, increase the holding company's consolidated non-thrift liabilities by five percent or more within a 12-month period, unless the holding company's non-thrift liabilities would be less than 50 percent of its consolidated tangible capital after the proposed issuance. We believe that this requirement would trigger a reporting obligation with respect to a substantial number of transactions by holding companies that rely on debt as a source of capital and funding. For example, in 2000, Merrill Lynch entered into over 350 transactions that would have triggered the notice requirement. None of those transactions, alone or in the aggregate, posed any risk to Merrill Lynch's thrift subsidiary.

The delay entailed in a 30- to 60-day prior review period would create a significant hurdle in Merrill Lynch's ability to adequately manage these safe and sound funding activities. Indeed, the proposed regulatory delays would impair the ability of a savings and loan holding company to act expeditiously in a favorable interest rate environment, creating barriers to precisely the type of activity holding companies should be encouraged to pursue. Moreover, the proposed requirements, if adopted, would impose a significant burden, not only upon holding companies, but also upon OTS staff. Preparation of notices would be time consuming for the subject institutions, but the burden of review by OTS staff would be multiplied many times over, as holding company after holding company submits applications for ordinary course transactions.

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[1] *See* Remarks of Ellen Seidman, Director, Office of Thrift Supervision for Presentation to the Exchequer Club of Washington, D.C. (January 17, 2001), http//www.ots.treas.gov/docs/87081.html; Remarks Prepared for Ellen Seidman, Director, Office of Thrift Supervision for the 11th Annual Seminar on International Finance (September 20, 2000), http://www.ots.treas.gov/docs/87078.pdf; Daigle, *In Focus: Nonbank Thrift Owners to Face More Scrutiny,* American Banker, October 16, 2000.

FEB-08-2001 17:33 MERRILL LYNCH 212 670 4525 P.04/07

Asset Acquisitions

The proposed rule would require 30 days' prior notice before a savings and loan holding company engages in or commits to engage in an acquisition of assets (other than cash, cash equivalents and United States government securities) that, when aggregated with all other transactions over a 12-month period, would equal or exceed 15 percent of the holding company's consolidated assets. We have several concerns with this requirement.

First, asset acquisitions would ostensibly include not only strategic acquisitions of businesses, but also acquisitions of assets in the ordinary course of business. For a financial services firm such as Merrill Lynch, ordinary course transactions include, among other things, purchases of securities under resale agreements, purchases of debt and equity securities for inventory purposes and purchases of securities and loans for investment purposes. Clearly, requiring notice of ordinary course transactions would hamstring the business of a large number of savings and loan holding companies and their non-thrift subsidiaries. This would be at odds with the concept of functional regulation and the requirements of the Gramm-Leach-Bliley Act.

Second, it would be impractical, if not impossible, for a holding company to give OTS 30 days' advance notice of strategic acquisitions. Timing, confidentiality and other sensitive aspects that are unique to strategic transactions limit a company's flexibility. To our knowledge, no other regulatory agency requires a regulated entity to provide notice of a transaction before the entity even "commits" to engage in a covered transaction. Even financial holding companies, for which Congress has provided closer regulation than unitary thrift holding companies, are only required to give notice of acquisitions after the fact. Savings and loan holding companies would be placed at a serious competitive disadvantage if they were required to obtain prior approval of an acquisition while similarly situated financial holding companies could proceed without such a requirement.

Finally, the requirement is redundant because of the requirement to notify OTS of debt transactions in excess of a specified amount and of transactions that would reduce capital below a specified threshold. Since an acquisition of assets in excess of 15 percent of consolidated assets will likely be financed with equity and an amount of liabilities, including newly issued debt, sufficient to activate the debt trigger, such debt trigger should then obviate the need for any asset-based restrictions. Attempting to otherwise review the quality of such asset acquisitions is inconsistent with Congress's clear determination that unitary savings and loan holding companies, like holding companies that own limited purpose trust companies, industrial loan companies or other specified banking entities, should be permitted to continue to affiliate with commercial enterprises. Transactions directly affecting thrifts are already adequately overseen through affiliate transaction, dividend and related restrictions. In the absence of such transactions, OTS should not be in the business of determining whether purchases of automobile parts by an automobile manufacture, inventory by a department store, or securities by a broker-dealer are in and of themselves "risky."

Recommendations

In light of the foregoing, we urge OTS to withdraw its proposed rulemaking. If OTS nonetheless determines to adopt the proposed rule in some form, we respectfully recommend the following modifications:

- The proposed rule should set forth specific standards for a Regional Director's determination that holding company transactions may pose a material risk to the safety and soundness of a savings association subsidiary. Those standards should be proposed for public comment and should focus on the direct relationship between the thrift and the holding company (*e.g.*, a transaction that causes the thrift's capital to fall below its required level). If, notwithstanding the foregoing, a holding company's financial condition is separately considered, a clear standard should be adopted (*e.g.*, its credit rating falls below single A as determined by a nationally recognized statistical rating organization).

- The proposed rule should provide an exemption for diversified savings and loan holding companies. We believe that it would be burdensome and intrusive for OTS to require notice of transactions that for many of these companies and their non-thrift subsidiaries are routine and conducted in the ordinary course of their business.

- The proposed rule should provide an exemption for savings and loan holding companies whose thrifts engage in limited activities that do not present the risks OTS seeks to address (*e.g.*, fiduciary operations). It should be noted, for example, that companies that own comparable limited purpose trust banks or credit card banks are specifically exempted from regulation under the Bank Holding Company Act, as amended.[2]

- The 10-percent threshold for tangible capital required to qualify for an exemption should be lowered. We believe that many well-run companies would not maintain that large a capital cushion. Even the Federal Reserve Board requires only a 5.5 percent ratio of primary capital to total assets for regulated bank holding companies.

- The five-percent threshold for an increase in non-thrift liabilities as a trigger of the notice requirement should be raised to at least 25 percent. We believe that an increase of five percent in a holding company's non-thrift liabilities over a 12-month period does not pose a threat to its subsidiary thrift. Companies that rely heavily on debt as a source of capital and liquidity may often increase their liabilities more than five percent in a 12-month period. In addition, this requirement essentially penalizes companies that depend on growth in balance sheet assets for growth in earnings. A high growth company would always exceed the five-percent threshold. Raising the threshold would reduce the burden on such companies and on OTS.

- The proposed rule should eliminate reference to asset acquisitions entirely, or at a minimum, define "acquisition of assets" in a manner that would include only major

[2] *See* 12 U.S.C. § 1841(c)(2)(D), (F).

FEB-08-2001 17:35 MERRILL LYNCH

acquisitions and that would exclude small acquisitions and assets acquired in the ordinary course of business.

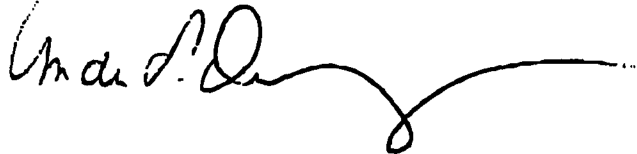
- If notice is required, it should be provided after the fact, rather than in advance. While OTS would not have the opportunity to disapprove a transaction, it would be able to monitor more closely the activities of non-exempt savings and loan holding companies and engage in discussions with those whose activities raise a concern.

Conclusion

In conclusion, we believe that the proposed rule would be burdensome for savings and loan companies to comply with and for OTS to administer. In addition, we believe that it would hamper the ability of many holding companies and their subsidiaries to finance and conduct their business activities. In essence, OTS could substitute its judgment for the business judgment of the boards of directors and elected officers of these companies without any indication that the company had acted in a manner that actually had a material adverse effect on the safety and soundness of the affiliated savings association. While many savings and loan holding companies might qualify for one or both of the proposed exemptions, OTS Regional Directors would have overriding authority to require notice filings. Accordingly, we urge OTS to withdraw the proposed rulemaking. If OTS nevertheless determines to adopt a form of the proposed rule, we urge it to consider the modifications suggested above.

Once again, we thank OTS for the opportunity to provide the above comments.

Very truly yours,



FEB-08-2001 17:36 MERRILL LYNCH 212 670 4503 P.07/07