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INFORMATION SERVICES DIVISION

Manager, Dissemination Branch
Information Management and Securities Division
Office of Thrift Supervision
1700 G Street NW
Washington, D.C. 20552

RE: Savings and Loan Holding Companies; Notice of Significant Transactions or Activities and OTS Review of Capital Adequacy; OTS No. 2000-91; 65 Federal Register 64392 (October 27, 2000)

Dear Sir or Madam:

The American Bankers Association ("ABA") appreciates the opportunity to comment on the above-cited proposed rulemaking requiring certain savings and loan holding companies to notify and receive approval from the Office of Thrift Supervision ("OTS") before engaging in particular types of transactions, acquisitions or activities. The ABA brings together all categories of banking institutions to best represent the interests of the rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies, savings banks, and savings and loan holding companies – makes ABA the largest banking trade association in the country.

Background

The proposed rule is the outgrowth of an evolution of the financial services industry to a more complex corporate structure with a variety of affiliates and businesses. The OTS-regulated, holding company population has long included diverse entities both within and without the business of banking. Because of this diversity, the OTS has pursued a regulatory approach that has focused on insulating or "fire walling" the insured savings association from pressures that may be exerted from a holding company under financial duress. This has historically worked. When there were situations that required supervisory intervention, the savings institution was a cohesive unit that could be sold separate and apart from the rest of the holding company structure. For many holding companies and savings associations, this traditional structure still exists. For others, the newer entrants to the OTS system, the savings bank is a business line that works closely with the other affiliates in the overall corporate family.

Because of the newer entrants, the OTS is concerned that its traditional approach to holding company regulation is inadequate and potentially poses a greater risk to the federal insurance funds. OTS does recognize that this concern does not extend to all of its holding companies, rather there are approximately 190 entities estimated by the OTS to be required to file pursuant to this rulemaking out of a population of over 531.[1] Further, the OTS notes that the Federal Reserve does not require prior notice of holding company acquisitions, but suggests that notice may be appropriate where a capital requirement is lacking.[2]

Description of Proposed Rule

The proposal is split into two parts: identification of those transactions subject to prior notification and approval and the exemptions to the notification requirement. Three types of debt transactions would be affected: the issuance, renewal or guarantee of a certain level of debt; any activity or transaction resulting in a reduction of 10% or more of the ratio of consolidated tangible capital to consolidated tangible assets; and certain types of asset acquisitions. The debt notice trigger would be tripped if the debt, when combined with all other debt transactions during the previous 12-month period, increases the amount of the holding company's consolidated non-thrift liabilities by five percent. The debt notice trigger would also be tripped if the holding company's consolidated non-thrift liabilities after the debt transaction would equal 50% or more of the holding company's consolidated tangible capital. In the second debt trigger, consolidated tangible capital would be defined as consolidated capital minus consolidated intangible assets and deferred policy acquisition costs.

Notice would also be required for certain types of asset acquisitions by the holding company or another subsidiary other than the regulated savings association. If the acquired assets (other than cash, cash equivalents, and securities or obligations unconditionally guaranteed by the U.S. Government) exceed 15% of the holding company's consolidated assets when combined with all other asset acquisitions during the previous 12-month period, prior notice would be required. Similar notice would also be required a proposed transaction, when combined with all other transactions over the prior year, would reduce the ratio of the holding company's tangible capital to consolidated tangible assets by ten percent or more. Individual notices may be avoided if the holding company submits a 12-month schedule of transactions, debt or acquisitions and receives supervisory approval.

Regional Directors would approve or disapprove the noticed transactions, depending on the material nature of the risk posed to the financial safety, soundness or stability of the subsidiary savings association; however, the criteria listed is more expansive. They include the extent to which debt is used and the terms of that debt, the impact on the risk to the overall holding company organization, whether the activity is self-funding or

[1] Estimated of number of respondents, 65 Fed. Reg. at 64399.

[2] 65 Fed. Reg. at 64393.

requires financial support from other subsidiaries including the savings association, and the effect of the transaction on the cash flow and liquidity of the savings association. The proposal notes that the Regional Directors may use additional criteria to approve or disprove the transaction.

A thirty day review period is triggered once the OTS receives "all required information" and the time period may be extended for an additional 30 days. While confidential treatment of this information may be possible through use of the OTS's application procedures (a matter subject to a recent, but not yet finalized, rulemaking), not all of an application receives confidential treatment, thereby delaying not only a competitively-sensitive transaction but also leaving an institution exposed to its competitors. There is no comfort present in the proposal (not even a cross-reference) for the potential competitive harm posed by filing confidential information.

Certain institutions would be exempt from the notice requirements outlined above. Those holding companies in which the regulated federal savings association represents less than 20% of the consolidated assets of the holding company would be exempt from the notice requirements. Similarly those holding companies with consolidated tangible capital of 10% or greater after completion of the transaction, acquisition or debt would also be exempt. The OTS believes that institutions in these categories pose minimal supervisory concerns and no prior notice would be necessary OTS Regional Directors would continue to have the supervisory flexibility to require notice even of exempt institutions. There is no discussion or process presented for those exempt institutions to challenge or remove themselves from a Regional Director's exercise of supervisory discretion.

General Comments

ABA disagrees with the approach outlined above and urges the OTS to withdraw the proposed rulemaking. The proposal, although replete with good intentions, will have the opposite effect. It will increase regulatory burden with no concomitant improvement in supervision. It will adversely impact the majority of traditional savings and loan holding companies while not impacting the newer entrants who pose the supervisory dilemma attempted to be addressed by the proposal. It is a blunderbuss in the age of rockets – a retread of debt budgets - an older supervisory tool abandoned as ineffective. It values lengthy supervisory process (30 day prior notice time period is not triggered until the notice is "deemed complete") at a time when nimbleness and responsiveness is *de rigueur* in order to maintain minimal competitiveness in the marketplace. ABA recognizes and understands the supervisory issues outlined in the proposed rule; however, the proposed solutions go beyond curing the concerns and threaten the competitive lifeblood of OTS-regulated institutions in a manner contrary to the legislative framework for savings and loan holding companies ("SLHCs").

1. The Proposal is Contrary to Gramm-Leach-Bliley.

The proposal's attempt to regulate the entire holding company structure appears to violate sections of the Gramm-Leach-Bliley Act ("GLBA") with regard to functionally regulated subsidiaries. OTS is prohibited by GLBA sections 112(b) and 113, 12 U.S.C. §§ 1831v, 1848a, to take action with respect to functionally regulated subsidiaries of SLHCs except in certain narrowly defined circumstances.[3] Specifically, these provisions require that the OTS act on a case-by-case basis with respect to a functionally regulated subsidiary of a SLHC, the approach that OTS has taken to date. Moreover, such provisions preclude the OTS from imposing requirements on or otherwise restricting the activities of functionally regulated subsidiaries of SLHCs unless two conditions are met: (i) the OTS's action is necessary to prevent or redress an unsafe or unsound practice or a breach of fiduciary duty by the functionally regulated subsidiary that poses a material risk to the financial safety, soundness, or stability of an affiliated thrift (or to the domestic or international payment system), and (ii) the OTS finds that it is not reasonably possible to protect effectively against the material risk at issue through action directed at or against the affiliated savings association. *See* 12 U.S.C. § 1848a(a). Significantly, these provisions also prohibit the OTS from requiring an SLHC to require its functionally regulated subsidiary to engage in or to refrain from an activity or transaction, unless the OTS could take such action directly against the functionally regulated subsidiary in accordance with the two statutory conditions described above. *See* 12 U.S.C. § 1848a(b).

The proposed rule would violate the above outlined GLBA sections by improperly requiring functionally regulated subsidiaries of SLHCs to receive OTS-prior approval of their transactions even though the statutory preconditions to such action were not satisfied. For example, nothing in the proposed rulemaking explains how a functionally regulated subsidiary engages in "an unsafe or unsound practice or breach of fiduciary duty that poses a material risk to the safety, soundness or stability" of the affiliated thrift simply by proposing to engage or engaging in a debt transaction, asset sale or other transaction covered by the rule.[4] Moreover, Congress' express limitation of OTS's authority over functionally regulated subsidiaries, except in cases of individualized determinations of risk, cannot be read to authorize a sweeping prior approval process for the entire industry.

Further, the proposed rulemaking fails to establish that OTS cannot "find that it is not reasonably possible to protect effectively against the material risk at issue through action

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[3] A "functionally regulated subsidiary" is any company, except a depository institution or depository institution holding company, that is a broker or dealer registered under the Securities Exchange Act of 1934, a registered investment advisor, properly registered by or on behalf of either the Securities and Exchange Commission or any State, with respect to the investment advisory activities of such investment advisor and activities incident to such investment advisory activities, an investment company that is registered under the Investment Company Act of 1940, an insurance company, with respect to insurance activities of the insurance company and activities incident to such insurance activities, that is subject to supervision by a State insurance regulator; or an entity that is subject to regulation by the Commodity Futures Trading Commission, with respect to the commodities activities of such entities or activities incidental to such commodities activities. *See* 12 U.S.C. § 1844(c)(5).

[4] *See First Nat'l Bank of Bellaire v. OCC*, 697 F.2d 674 (5th Cir. 1983) (holding that not having a certain level of capital is not, by definition, an unsafe or unsound practice).

directed at or against" savings associations generally.[5] There is no real analysis explaining why the risks OTS intends to cover cannot be addressed through direct regulation of savings associations. In fact, the history of SLHC regulation has demonstrated that the OTS has, for the most part, succeeded in its supervisory mission.

In addition, the proposal would authorize Regional Directors to require prior approval for transactions of functionally regulated subsidiaries of otherwise exempt SLHCs if a Regional Director "has concerns" relating to the SLHC's financial condition or the safety and soundness of its subsidiary savings association or that a transaction or activity "may pose a risk" to the safety, soundness, or stability of its subsidiary thrift. *See* Proposed Sections 584.110(b), 584.120(b), 65 Fed. Reg. at 64,400. These criteria fall far short of the statutory standards specified in Sections 112(b) and 113 of the GLBA.

Finally, the fact that the proposed rulemaking requires SLHCs, rather than functionally regulated subsidiaries, to file the required notices does not remove the proposed rulemaking from applicability of GLBA Sections 112(b) and 113. As noted above, Sections 112(b) and 113 forbid an agency to take action directly against a functionally regulated subsidiary but also forbid an agency from indirectly achieving the forbidden result by requiring a SLHC to require its functionally regulated subsidiary to engage or refrain from engaging in the conduct at issue. *See* 12 U.S.C. §§ 1831v(a), 1848a(b). Yet, the proposed rulemaking would allow indirect action against the functionally regulated subsidiary in just this manner.[6] As both a legal and practical matter, a functionally regulated subsidiary would have no choice but to comply with the requirements imposed upon its parent, including a requirement to refrain from engaging or committing to engage in a proposed transaction until OTS approval has been obtained.

Based on these failings alone, ABA urges the OTS to reconsider its approach afresh rather than attempt to turn back the clock and resurrect the abandoned supervisory tool of debt budgets. Times have changed; laws have changed. Old tools will not work, no matter how reconfigured.

2. <u>Inadequate Regulatory Flexibility and Paperwork Reduction Act Analyses.</u>

ABA believes that the proposal would disproportionately impact smaller institutions and their holding companies. OTS admits in its Regulatory Flexibility Act analysis that for 78% of its regulated population of holding companies, the savings association is the primary asset.[7] Of its holding companies, 88 holding companies fall within the SBA definition of "small" based on assets ($100 million or less in assets). Another 150 would

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[5] 12 U.S.C. §§ 1831v(b), 1848a(2).

[6] *See* 65 <u>Fed</u>. <u>Reg</u>. at 64,397 ("The proposed rule would apply to savings and loan holding companies *and subsidiaries of savings and loan holding companies* (other than savings association subsidiaries). A savings and loan holding company would be required to file a notice before it *or its non-thrift subsidiary* may engage in specified activities. While a subsidiary of a savings and loan holding company would not be required to file a notice, *OTS could, by disapproving a notice, prevent the subsidiary from engaging in certain proposed actions*.") (emphasis added).

[7] 65 <u>Fed</u> <u>Reg</u>. at 64397.

be classified as "small" based on revenues ($5 million or less in revenues). Of these two groups, the exemption for 10% tangible capital would exempt 81.3% of the 88 group or approximately 71 institutions and 70.5% of the 150 group or approximately 106 institutions. It is not clear how much overlap exists between the two groups. Because the percentages are over 50%, OTS claims that the proposal exempts a greater proportion of smaller holding companies than larger.

ABA respectfully submits that OTS misses the point of its analysis. A large percentage of a small number still means that a significant number of institutions and their holding companies are subject to the proposal. Further, of those smaller institutions subject to the proposal, the impact on their bottom lines and operations is disproportionately greater. The numbers used by OTS do not reflect the regulatory burden imposed and fail to accurately reflect the number of hours and costs associated with that burden. Because of that failure (and one acknowledged by OTS), the proposal lacks the necessary Regulatory Flexibility and Paperwork Reduction analysis.

3. Further Study is Required.

The admission by the OTS that it does not know the extent to which the proposal will impact its regulated population and their holding companies strongly suggests that another course of action is required. ABA urges the OTS to convene a task force of representatives of institutions and holding companies, industry experts both within the agency and outside, to take a fresh look at the supervisory issues presented and recommend a course of action. The issues are complex. It is, for example, unclear how this proposal may impact mutual holding companies. Further, the questions outlined by the proposal on the review of capital adequacy alone require greater input than the almost ANPR nature of the discussion contained in the proposed rule.[8] These issues pose fundamental, structural questions and deserve fuller treatment. ABA would be glad to be of assistance in a more inclusive and wider-ranging exploration of holding company capital issues.

Specific Questions

The proposed rulemaking poses a number of questions throughout the preamble. They include whether the exemption for institutions with tangible capital of 10% or more is the appropriate level, whether the exemption should be expanded to eliminate those holding companies that control only limited purpose savings associations, the appropriateness of the type of information required in the notice requesting prior approval, additional criteria to be used for approving or disapproving transactions, the relevance of the factors used to determine capital adequacy, and other questions designed to assist the agency with its mandates to write the regulation in plain language and to understand the burdens associated with the proposed rule. These are fundamental questions that support the

[8] 65 Fed. Reg. at 64395-64396. Indeed, the thought that OTS could issue a final rule on capital requirements for holding companies based on the limited discussion in another rulemaking is troubling and no doubt violative of the Administrative Procedures Act.

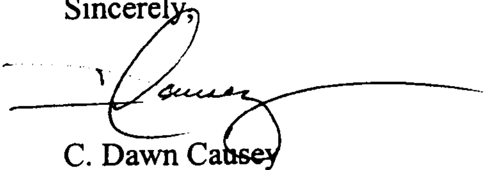
foundations of the proposal. Because ABA believes that the proposal is inadequately developed and requires further study, it is premature to attempt to answer the questions posed.

Conclusion

ABA urges the OTS to reconsider this regulatory action and withdraw the proposed rulemaking. Much more study, including the commissioning of an intra-industry task force with outside assistance, is warranted by the complexity and implications of the proposal. The issues presented deserve more; ABA stands ready to assist the OTS in developing a more targeted and effective approach to the newer corporate approaches to delivering financial services.

Your consideration of these comments is appreciated. If there are any questions on the issues raised by this letter, please do not hesitate to me at (202) 663-5434.

Sincerely,



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