INVESTMENT COMPANY INSTITUTE

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(24)

February 8, 2001

Manager
Dissemination Branch
Information Management Services Division
Office of Thrift Supervision
1700 G Street, N.W.
Washington, D.C. 20552

Re: Docket No. 2000-91

Dear Sir or Madam:

The Investment Company Institute[1] appreciates the opportunity to comment on the Notice of Proposed Rulemaking published on behalf of the Office of Thrift Supervision (OTS) in the Federal Register on October 27, 2000.[2] The Institute is interested in OTS' Notice because members of the Institute are, or are affiliated with companies that are, unitary savings and loan holding companies or functionally regulated subsidiaries of savings and loan holding companies within the meaning of the GLB Act.[3] Of particular interest to the Institute is the rule proposed by the OTS that would require a savings and loan holding company ("slhc") to notify and obtain approval from the OTS before such company or its non-savings association subsidiaries[4] engage or commit to engage in certain transactions (the "Prior Notice and Approval Proposal").[5]

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[1] The Investment Company Institute is the national association of the American investment company industry. Its membership includes 8,433 open-end investment companies ("mutual funds"), 491 closed-end investment companies and 8 sponsors of unit investment trusts. Its mutual fund members have assets of about $6.796 trillion, accounting for approximately 95% of total industry assets, and over 83.5 million individual shareholders.

[2] *See* 65 Fed. Reg. 64392 (Oct. 27, 2000).

[3] The Institute also notes that our members includes companies affiliated with institutions that, according to some press reports, are specific targets of the Prior Notice and Approval Proposal. *See* "Nonbank Thrift Owners To Face More Scrutiny," American Banker, Oct. 16, 2000 at p. 3.

[4] As proposed, this would include any subsidiaries that are "functionally regulated subsidiaries" within the meaning of Sections 113 and 112(b) of the Gramm-Leach-Bliley Act the ("GLB Act").

[5] *See* proposed Part 584. The second proposal would impose capital requirements on savings and loan holding companies. *See* 65 Fed. Reg. at 64395-96.

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The Institute recommends that OTS withdraw the Prior Notice and Approval Proposal.[6] As discussed in more detail below, application of this proposal to functionally regulated subsidiaries of slhcs would appear to violate Sections 113 and 112(b) of the GLB Act.

THE PRIOR NOTICE AND APPROVAL PROPOSAL

The Prior Notice and Approval Proposal would apply to all slhcs and their non-savings association subsidiaries. It would require prior notice and approval for a large number of transactions and activities, including the issuance, renewal or guarantee of debt that increases the amount of the slhc's consolidated non-thrift liabilities by more than 5%; the acquisition of assets amounting to more than 15% of the slhc's consolidated assets; and any other transaction that would reduce the slhc's ratio of consolidated tangible capital to consolidated tangible assets by 10% or more.[7] The proposal also would forbid an slhc or non-savings association subsidiary to commit to engage in or to consummate a proposed transaction whenever the Regional Director determines that the transaction "will pose a material risk to the financial safety, soundness or stability" of the holding company's savings association subsidiary.[8]

While the Prior Notice and Approval Proposal contains exceptions for an slhc whose aggregated thrift assets amount to less than 20% of the slhc's consolidated assets or which has consolidated tangible capital of 10% or more following the proposed transaction, these exceptions are effectively negated by two provisions contained in the proposal that permit the OTS to override them. One such override provision would require the slhc to provide prior notice and obtain the OTS' approval where a Regional Director "has concerns" relating to the financial condition of the shlc or the safety and soundness of the its savings association subsidiary.[9] The other would require prior notice and approval where a Regional Director informs an slhc that a transaction or activity "may pose a risk" to the financial safety, soundness or stability of its savings association subsidiary.[10]

SECTIONS 113 AND 112(B) OF THE GLB ACT

Sections 113 and 112(b) of the GLB Act are designed "to protect regulated subsidiaries, which already are subject to extensive regulation at the hands of their functional regulators, from additional and duplicative supervision" by federal banking regulators, including the

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[6] The Institute also recommends that the OTS withdraw its proposal to impose capital requirements on savings and loan holding companies. Indeed, in addition to the concerns expressed herein with the Prior Notice and Approval Proposal, we note that the OTS lacks the statutory authority to proceed with or adopt either proposal. *See* Comment Letter dated February 8, 2001 Re: Docket No. 2000-91 from Sidley & Austin.

[7] *See* proposed § 584.120(a).

[8] *See* proposed § 584.140.

[9] *See* proposed § 584.110(b).

[10] *See* proposed § 584.120(b).

OTS.[11] Taken together, Sections 113 and 112(b), in relevant part, forbid the OTS from taking any action with respect to a functionally regulated subsidiary of an slhc except (1) where such action is necessary to prevent or redress an unsafe or unsound practice or breach of fiduciary duty that poses a material risk to the financial safety, soundness or stability of an affiliated depository institution *and* (2) the OTS finds that it is not reasonably possible to protect effectively against the material risk presented by the unsafe or unsound practice or breach of fiduciary duty through action directed at or against the affiliated depository institution.[12]

Congress felt so strongly about the need for banking regulators to refrain from regulating the activities of functionally regulated subsidiaries of slhcs that it took steps to prevent even indirect regulation. Thus, Sections 113 and 112(b) also prevent the OTS from taking any action with respect to an slhc that requires the slhc to require the functionally regulated subsidiary to engage or to refrain from engaging in conduct unless the OTS could take such action directly against the functionally regulated subsidiary.[13]

ADOPTION OF THE NOTICE AND APPROVAL PROPOSAL WOULD VIOLATE THE GLB ACT

Adoption of the Notice and Approval Proposal would violate Sections 113 and 112(b) of the GLB Act. The rules contained in the Proposal contemplate that the OTS could "take action" with respect to functionally regulated subsidiaries of slhcs in two separate ways -- by requiring them to file a notice seeking permission to engage in certain transactions and by requiring them to refrain from engaging in such transactions under certain specified circumstances. The OTS has failed to establish, however, that either would be consistent with the statutory standards set forth in Sections 113 and 112(b).

As discussed above, to be lawful under the GLB Act, the OTS may take action against functionally regulated subsidiaries of an slhc *only* where the "action is *necessary* to prevent or redress an *unsafe or unsound practice* or *breach of fiduciary duty* that poses a material risk to the financial safety, soundness or stability of an affiliated depository institution."[14] Yet, nothing in the Proposal addresses how a functionally regulated subsidiary engages in an unsafe or unsound practice or breaches a fiduciary duty by proposing to engage in a covered transaction. This is true even where the proposed transaction may have one of the characteristics specified in the Proposal, such as increasing an slhc's consolidated non-thrift liabilities by 5% or increasing the slhc's assets by 15%. As previously held by a federal court, merely identifying

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[11] *See* H. R. Rep. No. 106-74 Part I, 106th Cong., 1st Sess. 131 (Mar. 23, 1999). *Accord* H. R. Rep. No. 106-74 Part 5, 106th Cong., 1st Sess. 146 (June 15, 1999); S. Rep. No. 106-44, 106th Cong., 1st Sess. 26 (Apr. 26, 1999).

[12] *See* 12 U.S.C. §§ 1848a(a), 1831v(a)(3).

[13] *See* 12 U.S.C. §§ 1848a(b), 1831v(a)(3).

[14] *See* 12 U.S.C. §§ 1848a(a)(1), 1831v(a)(3)(emphasis supplied).

characteristics of a transaction does not provide any evidence that the transaction constitutes either an unsafe or unsound transaction or a breach of fiduciary duty.[15]

Even assuming, however, that the OTS somehow could satisfy the first statutory pre-condition, Sections 113 and 112(b) still would prevent adoption of the Proposal because the second statutory pre-condition remains unsatisfied. Specifically, Sections 113 and 112(b) require not only the existence of an unsafe or unsound practice or breach of fiduciary duty posing a material risk, but also, that the OTS *"find"* that it is not reasonably possible to protect effectively against the material risk through action directed at or against the holding company's savings association subsidiary or against savings associations generally.[16] The OTS Notice fails to specifically find that the risk cannot effectively be addressed through action at the savings association level. As such, the Proposal is not in accordance with the limits placed on the OTS' authority under the GLB Act.

The provisions of the proposal authorizing the Regional Directors to apply the proposed rule to slhcs that otherwise would fall outside the scope of the rule by virtue of the asset or capital exceptions similarly contravene Sections 113 and 112(b) of the GLB Act. Under the GLB Act, it is not enough that a Regional Director "has concerns" about the financial condition of an shlc or thinks that a transaction "may pose a risk" to a holding company's savings association subsidiary. Instead, the GLB Act permits agency action only in the very narrow circumstance where both of the statutory preconditions to action are present. Amorphous "concerns" and unspecified potential "risks" plainly do not satisfy the statutory standards.

In addition, the circumstances under which the proposal would permit disapproval of proposed transactions is inconsistent with Sections 113 and 112(b) of the GLB Act. This is because the proposed rule would permit disapproval whenever a Regional Director determines that the transaction "will pose a material risk to the financial safety, soundness or stability " of the holding company's savings association subsidiary.[17] By contrast, however, Sections 113 and 112(b) of the GLB Act permit action only where disapproval "is *necessary* to prevent or redress an *unsafe or unsound practice* or *breach of fiduciary duty* that poses a material risk to the financial safety, soundness or stability of an affiliated depository institution" *and* that "it is not reasonably possible to protect effectively" against the material risk *presented by the unsafe or unsound practice or breach of fiduciary duty* through action directed at or against the holding company's savings association subsidiary or against savings associations generally.[18]

The Proposal also contravenes the requirements of Sections 113 and 112(b) by vesting the authority to make the determinations described in the preceeding two paragraphs in the various OTS Regional Directors. Sections 113 and 112(b) require action by the agency, not by

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[15] *See First National Bank of Bellaire v. OCC*, 697 F.2d 674 (5th Cir. 1983) (rejecting proposition that having a certain capital level in and of itself constitutes an unsafe or unsound practice).

[16] *See* 12 U.S.C. §§ 1848a(a)(2), 1831v(a)(3) (emphasis supplied).

[17] *See* proposed § 584.140 (emphasis supplied).

[18] *See* 12 U.S.C. §§ 1848(a), 1831v(a)(3) (emphasis supplied).

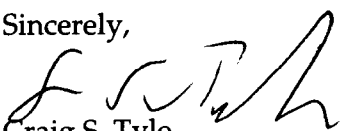
agency staff. By their terms, they permit action only where "the Board" or another "Federal banking agency" determines that the statutory standards are satisfied.

Finally, it is of no moment that, in transactions involving functionally regulated subsidiaries of slhcs, the proposal places the obligation to file a notice upon the parent slhc instead of upon the subsidiary. Sections 113 and 112(b) of the GLB Act expressly forbid an agency, such as the OTS, from indirectly achieving the forbidden result by imposing upon a holding company regulatory requirements aimed at the subsidiary.[19] Notwithstanding this express Congressional prohibition, the OTS readily admits that its proposal would authorize such indirect action against the functionally regulated subsidiary in just this manner.[20] As such, the proposal is not in compliance with the limits placed on the OTS' authority under the GLB Act.

CONCLUSION

The prior notice and approval requirements that the OTS attempts, through this proposal, to impose upon functionally regulated subsidiaries of an slhc are precisely the type of requirements that, in connection with the enactment of the GLB Act, Congress considered and rejected. Since Congress has spoken, it is not the province of the OTS to revisit the matter. As noted by the U.S. Supreme Court, a federal agency's "rulemaking power is limited to adopting regulations to carry into the effect the will of Congress as expressed in the statute. . . "[21] Accordingly, the Prior Notice and Approval Proposal should be withdrawn.[22]

Sincerely,



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[19] *See* 12 U.S.C. §§ 1848a(b), 1831v(a)(3).

[20] *See, e.g.*, 65 Fed. Reg. at 64397 ("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 supplied).

[21] *See Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 374-5 (1986).

[22] As discussed above, we additionally recommend that the portion of the proposal relating to the capital requirements of an slhc be withdrawn as outside the OTS' statutory authority.