Robert L. Andersen
Senior Vice President and
Deputy General Counsel
Direct Dial 704 374-2215
Fax: 704 715-4494
Email: bob.andersen@wachovia.com

September 30, 2003

SENT VIA ELECTRONIC MAIL AND COURIER

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., N.W.
Washington, D.C. 20551
Attn: regs.comments@federalreserve.gov

Re: Docket No. OP-1158, Anti-Tying Restrictions of Section 106 of the Bank Holding Company Act Amendments of 1970.

Dear Ms. Johnson:

As a leader in the financial services industry, Wachovia Corporation[1] ("Wachovia") welcomes the opportunity to comment on the proposed interpretation and supervisory guidance issued by the Board of Governors of the Federal Reserve System (the "Board") on the anti-tying restrictions of Section 106 of the Bank Holding Company Act Amendments of 1970. 68 Fed. Reg. 52,024 (Aug. 29, 2003) (the "Release"). We strongly support the Board's efforts to provide guidance on this topic at this time. We are pleased that in providing this interpretation, the Board has recognized and accounted for the evolution of the banking industry since the adoption of Section 106

[1] Wachovia Corporation (NYSE:WB) is one of the largest providers of financial services to retail, brokerage and corporate customers throughout the East Coast and the nation, with assets of $364 billion and stockholders' equity of $32 billion at June 30, 2003.

and has attempted to provide guidance consistent with the current financial services landscape.

Specifically, Wachovia is pleased that the Board has proposed an interpretation of Section 106 that (i) recognizes the impact that customer-initiated and customer-driven tying arrangements have on banks' actions under Section 106; (ii) recognizes the importance of relationship banking in the context of Section 106; and (iii) provides meaningful examples of products considered "traditional bank products" under Section 106.

We also take this opportunity to note that we subscribe to and, unless noted below, endorse the viewpoints expressed in the industry comment letters submitted by the ABA Securities Association (the "ABASA Letter") and The New York Clearing House Association, L.L.C. (the "Clearinghouse Letter"). Our comments will focus on specific areas of the proposed interpretation and supervisory guidance which we find to be of particular concern or which we hope can be further clarified to assist banks in their efforts to comply with Section 106.

Specific Issues

1. Certain Foreign Exchange, Interest Rate Swap or Other Derivative Transactions Should be Exempt from Section 106

Wachovia previously has written to the Board requesting an exemption from Section 106 for tie-ins between (a) loans and (b) foreign exchange, interest rate swap and other derivative transactions related to loans made or arranged by its subsidiary banks.

Wachovia requests that the Board use its exemptive authority under Section 106 to permit any bank to extend credit, lease or sell property of any kind, or furnish any service (each a "*bank product or service*"), or to fix or vary the consideration for any of the foregoing, on the condition or requirement that a client (or its affiliate) obtain from, or provide to, the bank (or an affiliate of the bank) a foreign exchange, interest rate swap or other derivative product or service ("*FX or derivative bank product or service*"), thereby treating FX or derivative bank products and services as traditional bank products and services.

First, this exemption would allow banks to present to customers a combination of FX or derivative bank products and services combined together as one offering, a practice we believe is entirely consistent with the purposes of Section 106 and should be permitted without qualification. Second, it would permit banks to combine any other type of bank product or service (including loans, discounts, deposits and trust services) with an FX or derivative bank product or service.

In the case of such tying arrangements involving one of the four statutory traditional bank products or services (i.e., loans, discounts, deposits or trust services), Wachovia believes that, as a condition to allowing such arrangements, the Board could require that the FX or derivative bank product or service be closely related to one of these four bank products or services. Assuming the Board determines that such a requirement is necessary, we would urge the Board to apply an objective standard. For example, the Board could require that when any FX or derivative bank product or service is combined with one of these four statutory traditional bank products or services, then the FX or derivative bank product or service must be obtained or provided for one of the following purposes:

(i) acquiring, disposing of, or settling the other bank product or service or a transaction executed by the client (or by its affiliate) in connection with the other bank product or service;

(ii) hedging, managing or altering a risk, return or other characteristic of the other bank product or service or an asset or liability acquired, financed, refinanced or disposed of in connection with the other bank product or service, whether that risk or return (or other characteristic), or that asset or liability, is that of the client (or its affiliate) or that of the bank (or its affiliate); or

(iii) structuring an overall transaction of which the other bank product or service and the FX or derivative bank product or service each forms a part.

FX and derivative bank products and services have become well established and essential parts of the products and services offered by banks,. When an FX or bank product or service is tied to an underlying loan, discount, deposit or trust service, such arrangements represent an appropriate extension of the underlying bank product or service itself.

This exemptive approach would recognize that FX and derivative bank products and services have become traditional bank products and services for the purposes Congress intended, allow banks to combine FX or derivative bank products and services into a single offering of such products and services, and permit banks to compete with investment banks in respect of tie-ins to other types of products and services in a manner consistent with the purposes of Section 106.

We also believe that the Board can exercise its exemptive authority for such arrangements without any finding that any individual FX or derivative bank product or service is an integral part of one of the four statutory traditional bank products or services. There is nothing in Section 106 or its legislative history to suggest that Congress meant for the Board to limit exemptions to products that are integrated with each other. An integration test is helpful to determine by statutory interpretation whether or not a particular tying arrangement falls within Section 106. When the Board grants an exemption, however, we do not believe that an integration test is necessary or relevant. Moreover, to require that the tied products or services be sufficiently integrated would call for a case-by-case analysis, potentially creating legal uncertainty as to whether or not this requirement has been met. We believe that our suggested purpose-based approach more appropriately views providing an FX or derivative bank product or service along with one of the four statutory traditional bank products or services as an extension of the underlying bank product or service without having to find that they are sufficiently integrated.

For the same reason, we urge the Board to avoid adopting a broad-based exception or interpretation that views any tie-in for a FX or derivative product or service as a single product. That would appear to require a fact-specific or product-specific determination, an approach we believe would be as impractical as an integration test (in the absence of more definitive guidance from the Board). Moreover, maintaining the separateness of interest rate swaps from the underlying loans they hedge has proven to be an

important legal doctrine in cases involving allegations that swap payments constitute prohibited unmatured interest in bankruptcy (e.g., Thrifty Oil Co. v. Bank of Am. Nat'l Trust & Savs. Ass'n, 310 F.3d 1188 (9th Cir. 2002)) or that swaps do not survive loan prepayment. Any finding by the Board that these swaps and loans constitute a single product for purposes of Section 106 could fuel efforts by adverse claimants to prove they should be treated as a single transaction for other purposes. This is an important reason for the Board to treat both loans and swaps as traditional bank products by issuing an exemption instead of considering them a single product pursuant to a statutory interpretation.

We are confident that an exception treating FX and derivative bank products and services as traditional bank products and services in the manner outlined above would be entirely consistent with the purposes of Section 106.

2. Certain Products Are So Inter-Related Under Certain Circumstances That They Should Not Be Considered Separate Products

The Board has properly recognized that an essential element of a tying arrangement is that the tying involve two or more separate products. In a footnote, the Board states that "…as a general matter, two products are separate and distinct for purposes of section 106 only if there is sufficient consumer demand for each of the products individually that it would be efficient for a firm to provide the two products separately" (footnote 23 of the Release). This standard is very difficult to apply and would require a bank to conduct significant economic diligence relating to market demand or to engage in significant subjective judgment. Any conclusions based upon this standard could be easily challenged or second-guessed. Accordingly, banks can take little comfort in relying on decisions made pursuant to their interpretation of this standard.

Wachovia urges the Board to adopt a more pragmatic approach to product separateness. We endorse the standard advocated in the Clearinghouse Letter, that the products are, for the purposes of Section 106, one product if they are so "functionally integrated" that it is reasonable for a bank to determine that they be sold as one product. As a practical matter, it would be reasonable to conclude that the products are functionally integrated if, the customer would not be interested in obtaining one

product if it did not receive the other. Under this "functionally integrated" standard it would be clear that the following products could be viewed as one product for anti-tying purposes:

- Trust services and certain operational support services
- Loan arranging and loan commitments
- Letters of credit and municipal bond placement or underwriting services

We also believe that a logical corollary to the "functionally integrated" standard would be that when the customer is indifferent to receiving one single product versus two functionally integrated products, the two functionally integrated products can be viewed as a single product for purposes of Section 106. For example, a borrower seeking debt financing for an acquisition is indifferent as to whether or not the debt financing comes in the form of one loan, two loans (senior and subordinated) or some mix of loans and bonds. Accordingly, banks should be able to offer acquisition financing as one product (since that is how the customer views its financing need) and negotiate terms, including price and availability, on the entire package. This would be consistent with the market's perception that acquisition financing is a single, integrated product.

The "functionally integrated" test is consistent with the intent of Section 106. The anti-tying rules are designed to prevent a bank from using its leverage to coerce a customer to take a second unwanted product. If, however, the customer views the products as so functionally integrated that obtaining only one of the products is of no value to the customer, then there is no coercion on the part of the bank. Similarly, if the customer is indifferent as to whether or not the product it receives, is in the form of a single product or a product with two components, then there would seem to be no coercion on the part of the bank in offering the two components in a combined package.

3. Mixed-Product Arrangements

As mentioned previously, Wachovia is very pleased that the Board has recognized the legitimacy of "relationship banking" and has properly concluded that certain aspects of relationship banking do not constitute anti-tying violations. We are particularly pleased by (i) the Board's express statement that "section 106 does not require a bank to extend credit or provide any other

product to any customer"; (ii) the Board's recognition that banks can make determinations to extend credit based on the profitability of the customer relationship to the bank; and (iii) the Board's recognition of the legitimacy of mixed-product arrangements. We view such arrangements as consistent with the traditional bank product exception, providing customers with more choices and thereby advancing the purpose of the Section 106.

We understand the Board's concern that such mixed-product arrangements not result in otherwise impermissible tying arrangements. We strongly support, however, the position espoused in both the ABASA and Clearinghouse Letters that the procedures suggested by the Board to determine whether or not the customer has a "meaningful" choice pose additional, unwarranted burdens on banks and are very problematic. Such procedures would require the bank to make a case-by-case determination of each customer's need for specific traditional bank products; create significant compliance and diligence burdens; require a bank to make subjective determinations as to a customer's legal obligations to other providers; and expose the bank to "second-guessing" by customers. Such customer-specific analysis of meaningful choice has never been part of the traditional bank product exception nor the combined-balance discount exception. Instead, the focus of the combined-balance discount scenario requires that the bank product be given at least equal weight as non-bank products.

To allow proper utilization of mixed-product arrangements, we would urge that the Board create several safe harbors within which the bank can utilize mixed-product arrangements. The following are safe harbors that Wachovia would recommend:

- Class of Customer Product Need Profiles – We believe that the bank should be able to develop a traditional bank product "needs profile" for a class of customers. (For example, a single needs profile could be developed for all industrial or manufacturing companies with more that $100 million in revenues). A needs profile would conclusively establish the banks good faith belief that the traditional bank products contained in such profile provide a meaningful choice for customers in that class.

The Board has implied in the Release that this may be an acceptable approach to meaningful choice, citing as a factor in confirming the bank's good faith belief the "…types and amounts of traditional bank products typically required or obtained by companies that are comparable in size, credit quality and nature, scope and complexity of business operations…". We urge the Board to go further and elevate this "class of customer" approach from a "factor" to a safe-harbor.

- Highly Sophisticated Corporate Customers – We would urge the Board to consider exempting from the "meaningful choice" diligence and documentation process certain very large, sophisticated corporate customers. There are two reasons for this exclusion. First, these customers are of such size and utilize such large quantities of traditional bank products that, provided such traditional products are on the menu of bank products offered, it can be presumed conclusively that such companies could meet any return threshold using only traditional bank products. Second, it has been our experience that banks do not have the ability to coerce, or otherwise exercise leverage, on these customers. Accordingly, excluding these customers from any diligence and documentation requirements would have no adverse impact.

- Fee Income Approach – Wachovia is (and, we believe, most other financial institutions are) able to characterize hurdle rate deficiencies in terms of actual dollar amounts of fee income. That is, by reviewing a total customer relationship, a bank can determine what amount of additional fee income is needed in order to meet profitability hurdles. We believe that the "meaningful choice" criterion would be conclusively met if the bank (i) communicates to the customer the fee amount deficiency; (ii) provides the customer a list of all fee income products and services offered by the bank and its affiliates (which would include both traditional and non-traditional bank products); and (iii) asks the customer to purchase any products and services that they wish, provided additional fee income at least equal to the fee deficiency amount is received. We believe this

model would provide significant benefits to both customers and the bank while preserving the intent of Section 106. Customers would not be compelled to purchase any non-traditional bank products that they did not desire to purchase. Instead, customers could pay the bank the full fee deficiency amount to obtain desired products only. Under this approach a dollar of fee income from any source would be considered equal to a dollar of fee income from any other source; all products would be equally rated. Banks could offer their full product menu, providing the widest range of choices available, and no additional documentation would be necessary. This approach would give a customer a clear understanding of the amount of fee income the bank needs to meet its profitability hurdles and provide the customer the maximum amount of product flexibility to meet such hurdles.

- Sophisticated Individual Investor. The Release suggests a presumption against the ability of a bank to offer mixed-product arrangements to individuals. The bases for the Board's presumption are that (i) bank products for individuals typically are standardized and (ii) individuals have less bargaining power than businesses and are more susceptible to subtle pressure by the bank. For the purpose of this letter, Wachovia will assume that such presumptions are generally accurate. However, in our view, these presumptions are inaccurate with respect to sophisticated, high net worth individuals. High net worth individuals are offered, and typically demand, products tailored to meet their individual needs. Because they are highly desirable customers, they have significant bargaining power with banks. Because they are financially sophisticated, they use this bargaining power effectively. Accordingly, we would request that the Board take the position that there is no presumption against the ability of banks to offer mixed-product arrangements to high net worth individuals.

As the Board has recognized, active and competitive financial holding companies benefit the financial services industry by increasing competition. Wachovia believes that the adoption of safe harbors as described above would promote efficiency and minimize the resources which would be

needed to document meaningful choice for purposes of the mixed-product arrangement analysis. Wachovia believes this is necessary to maintain the domestic and international competitiveness of bank holding companies in this era when less-regulated competitors have succeeded in developing products and services traditionally provided by bank holding companies and their subsidiaries and can tie products and services without regard to the limitations imposed under Section 106.

4. Customer-Initiated Ties

An essential element of a Section 106 violation is that a bank must require a customer to obtain the tied product from the bank or an affiliate in order to obtain the customer's desired product from the bank. The Board recognizes that (i) the antitrust laws distinguish between a seller imposed arrangement and one voluntarily sought by the customer, and (ii) that an analogous distinction is present in Section 106. Therefore, the Release declares that Section 106 is not violated if it is the customer, rather than the bank, that imposes a condition or a requirement that ties the desired product to another product.

Although we are pleased that the Board recognizes the economic and bargaining power that customers can exercise when negotiating with banks, we are concerned that the Release does not make it clear that banks are free to negotiate the terms of tying arrangements voluntarily imposed by customers. The Board should clarify that once a customer voluntarily imposes a condition on a product's availability or the pricing thereof, the bank is free to negotiate the terms of that condition, or any portion thereof, including both the products the customer is conditioning, and the pricing of any such products. Because the Board recognizes the impact that customer's actions can play in the Section 106 analysis, we urge the Board to clarify that once the customer has initiated a tie, the bank is free to follow the customer down that path and fully negotiate the terms of the transaction without concern that it will inadvertently violate Section 106.

5. Traditional Bank Products.

We find it very helpful that the Board has provided a list of products that it considers to be "traditional bank products". We ask the Board to take a broad view of what constitutes a traditional bank product, mindful of the continued evolution of the financial services industry and the services banks provide.

For example, we applaud the Board's recognition of credit default swaps (a product that did not exist when Section 106 was written) as a traditional bank product. Consistent with that view, we would request that the Board, either through its exemptive authority or by statutory interpretation, consider the following products "traditional bank products" for the purpose of Section 106:

- Trust Services – While the list proposed in the Release is non-exclusive, we would still the Board to articulate a broader definition of trust services. At minimum, the Board should expressly include any services performed by a bank's corporate trust department, institutional trust department or ERISA trust department or by any bank affiliate which is a registered investment advisor under the Investment Advisor Act of 1940.

- Foreign Exchange – We appreciate the Board's solicitation of comments on this issue. Subject to our discussion earlier in this letter, we believe foreign exchange should be considered a traditional bank product the same as other cash management products. Banks have had a long history of providing foreign exchange services and are looked upon as the traditional providers of foreign exchange products and services.

- Interest Rate Swaps and Other Derivatives – Subject to our comments earlier in this letter, we believe such products should be considered traditional bank products. Interest rate swaps and similar derivative products have become an integral component of the products and services customers require from banks.[2]

[2] To the extent the Board broadens the definition of "traditional bank product" to include products such as foreign exchange products and certain derivatives, the "meaningful choice" analysis becomes more workable.

We appreciate the opportunity to comment on this proposal. Should you wish to discuss this letter, feel free to contact Vincent Altamura, Senior Vice President and Assistant General Counsel (704-383-4903) or Robert Andersen, Senior Vice President and Deputy General Counsel (704-374-2215) at your convenience.

Very truly yours,

/S/Robert L. Andersen

Robert L. Andersen

cc: via electronic mail
Wachovia Corporation:
Mark Treanor, Senior Executive Vice President and General Counsel
Michael Watkins, Senior Vice President and Deputy General Counsel
Vince Altamura, Senior Vice President and Assistant General Counsel