MARIETTA M. MAXFIELD
Vice President---Special Counsel
1980 Post Oak Blvd., Suite 748
Houston, Texas 77056
Direct: 713-625-8258
Fax: 713-552-9523
E-Mail: mmaxfiel@stewart.com

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Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW.
Washington, DC 20551

By E-Mail to regs.comments@federalreserve.gov;
By Fax to the Office of the Secretary at 202-452-3819;
By Fax to the Office of the Secretary at 202-452-3102

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

Dear Ms. Johnson:

Stewart Title Guaranty Company ("Stewart Title") is a title insurance company that provides title insurance policies written by over 6,000 title insurance agencies in 49 states in the United States. Many national banks are customers of Stewart Title Guaranty Company and are impacted by the Federal Reserve Board's Interpretation of Section 106. Stewart Title timely files this Public Comment in Response to the invitation of the Federal Reserve Board.

The purpose of these comments is to briefly summarize why the Board's proposed interpretation is impermissible under current law; and to show that the interpretation does not comport with the language, purpose, or legislative history of section 106.

Second, our comments touch on the negative impact on small businesses, such as title insurance agencies, resulting from the Board interpretation that carves out a new arena of lender exemption from statutory anti-tying restrictions, contrary to the purpose and legislative history of section 106.

Third, our comments discuss detriment to consumers that results from the Board Interpretation that allows lenders to offer mixed-product arrangements.

Stewart Title maintains that congressional action is required to determine the true impact of the policy the Board is seeking to reach by issuing this interpretation.

Section 106 of the Bank Holding Company Act, 12 U.S.C. § 1972(1) (2003), prohibits banks from extending credit or selling a good or service "on the condition or requirement" that the customer take an additional action set forth in the statute. For example, a bank may not condition the extension of credit on the customer's purchase of title services. This prohibition was designed to regulate tying arrangements involving credit more stringently than they would be under the general antitrust statutes. S. Rep. No. 1084, 91st Cong., 2d Sess., *reprinted in* 1970 U.S.C.C.A.N. 5519, 5558 (Letter of Assistant Attorney General Richard McLaren).

In its interpretation of section 106, however, the Board seeks to insulate banks from liability by requiring a two-step test that is supported neither by law nor by the Act's legislative history. Alarmingly, the Board's proposed interpretation would allow banks to *imply* to customers that additional products or services must also be purchased, provided that they *actually* need not be purchased. This would have the undesirable effect of causing many consumers to be misled and to enter into transactions involuntarily. So long as the bank stopped short of *expressly* requiring the two purchases, it could force the consumer into an unwanted expenditure.

This approach would defeat the Act's purpose. The Board itself cites legislative history indicating that a section 106 violation occurs whenever "the customer has not voluntarily entered into the transaction." Furthermore, the legislative history indicates that Congress intended to prohibit implicit, as well as explicit, conditions:

> Tie-ins occur where a customer is forced *or induced* to accept other products and services along with that product which he seeks. Such tie-ins result from actual coercion by a seller *or from a customer's realization* that he stands a better chance of securing a scarce and important commodity (such as credit) by 'volunteering' to accept other products or services rather than seeking them in the competitive market place. *In either case, competition is adversely affected*, as customers no longer purchase a product or service on its own economic merit.

Conf. Rep. No. 1747, 91st Cong., 2d Sess., *reprinted in* 1970 U.S.C.C.A.N. 5561, 5569 (emphasis added).

Moreover, the Board's two-step approach to tying arrangements -- that there be a "requirement" of two purchases and that such requirement be "imposed" by the bank -- defies logic. By definition, requirements are imposed. And they may be imposed either explicitly or implicitly. Indeed, in its discussion of coercion, the Board goes to great lengths to make clear that implicit coercion is prohibited ("prohibited coercive actions may be explicit or implicit"). Yet in its discussion of the existence of an actual requirement, the Board states that impermissible tying will not exist if the customer has a choice not to purchase the additional

product. This disconnect leads to the absurd result that a bank engaging in implicit coercion would not violate section 106 if, unbeknownst to the customer, there is no actual requirement.

As the Board is aware, this two-step test was expressly rejected by the Fifth Circuit in *Dibidale of Louisiana, Inc. v. American Bank & Trust Co.,* 916 F.2d 300 (5th Cir. 1990). There, based on a substantial review and discussion of the legislative history, the Court dismissed the view of coercion that the Board proposes to adopt. The *Dibidale* Court noted that restricting section 106 to tying arrangements in which a customer is "literally forced [to purchase an additional service] … would vitiate that section's intended role." *Id.* at 306. Like the Conference Report language cited above, the Fifth Circuit's holding in *Dibidale* would prohibit not just explicit conditions or requirements, but implicit conditions or requirements as well.

By contrast, the Board relies on case law that fails to support its position. In *Duryea v. Third Northwestern Nat'l Bank*, 660 F.2d 823 (8th Cir. 1979), the Eighth Circuit affirmed the trial court's finding that the customer "was not coerced, required *or encouraged* by the Bank" to purchase the tied product. *Id.* at 826 (emphasis added). Thus, the Eighth Circuit recognized that when banks are dealing with consumers, even strong "encouragement" can result in a tying arrangement. The Eighth Circuit did not hold that violations of section 106 occur only where a bank has expressly required the additional purchase.

Furthermore, our view finds additional support in text cited by the Board. For example, no tying arrangement exists "unless the defendant improperly imposes conditions that explicitly *or practically* require buyers to take" additional action. 9 Phillip Areeda, *Antitrust Law* at 1752 (1991) (as cited at 68 Fed. Reg. 52028) (emphasis added). As a practical matter, bank customers who need a loan or other bank service for a major purchase or other transaction, often on a tight schedule, will not feel that they have a choice when the bank suggests strongly that they buy a particular product or service.

In short, the Board's proposed interpretation is impermissible under current law. The interpretation does not comport with the language, purpose, or legislative history of section 106.

Congress authorized the Federal Reserve Board to grant additional exceptions from the statute's prohibition, by regulation or order, only if "the Board determines the exception 'will not be contrary to the purposes of section 106.'" *See* 68 Fed. Reg. 52024, 52030. By enlarging the scope of the exception by examples of mixed –product arrangements that avoid statutory prohibitions (Id., Part IV.A.2.*Mixed-product arrangements*), the Board Interpretation allows banks to circumvent the legislative purpose of the statute. In 1970, during the framing of the statute, "Congress expressed concern that banks might use their ability to offer bank products-credit in particular-in a coercive manner to gain a competitive advantage in markets for non-banking products and services (such as insurance sales)." *See* the *Federal Register*/ Vol. 68, No. 168/Friday, August 29, 2003/Notices, 52024, footnote 4, "S. Rep. Ho. 1084, 91st Cong., 2d Sess.

(1970)." "The Statute is intended to prevent banks from using their ability to offer bank products, credit in particular, in a coercive manner to gain a competitive advantage in markets for other products and services." See 68 Fed. Reg. 52024, 52025 *I. Introduction*.

The Board Interpretation, Part IV, A. 2. allows the Bank to offer mixed - product arrangements to the customer. In a mixed–product arrangement, for example, the bank conditions the renewal of a backup credit facility, at a favorable interest rate, on customer choice to purchase a specified amount of traditional bank products or non-traditional bank products such as insurance, securities underwriting or strategic advisory services from the bank. The bank is requiring "more business" from the corporate customer to meet an internal threshold of profitability (called the "hurdle rate"). The Board Interpretation states that there is no "bank coercion" in the sense of a Section 106 violation, if the corporate customer can meet the "hurdle rate" by choosing only traditional bank products. The corporate customer that chooses insurance to meet the "hurdle rate" cannot later complain that the Bank was in violation of Section 106 by conditioning the loan on this choice, because traditional bank products were included in the option.

Transactions purporting to be "mixed- product arrangements" may offer only "paper choices", not real choices. If a corporate customer does not need the traditional bank products included in the option, or is under contract to purchase these bank products elsewhere, the customer is faced with the "real" choice to purchase the non-bank product, such as insurance, to meet the "hurdle rate" or lose the lower interest rate. In these instances, the bank essentially is conditioning the lower interest loan on a purchase of non-bank products, such as insurance, contrary to the purpose of the statute.

The Board Interpretation negatively impacts the insurance marketplace by encouraging banks to market insurance products to bank customers, both corporate and individuals, and allows big lenders to capture business previously provided by small businesses, including the 6,000 title insurance agencies which write Stewart Title Guaranty policies.

Stewart Title is concerned that other federal agencies such as the Office of the Comptroller of the Currency ("OCC"), and the Department of Housing and Urban Development ("HUD") are proposing rules that result in diverting billions of dollars in annual insurance revenues from small businesses (such as title agencies), to big lenders, the national banks. Although the intent stated in these rules is to provide lower cost to the consumer and to promote consumer convenience, the consumer impact of transferring the control of settlement services to national banks is hidden costs and fees and a deficit of real choices and disclosures to the consumer. For a discussion of the negative impact on small businesses affected by the proposed RESPA Rule (Docket No. FR-4727-P-01; 67 Fed. Reg. 49134 (July 29, 2002), go to http://www.alta.org to see the Supplement to the Public Comment to the Department of Housing and Urban Development ("HUD"), filed October 28, 2002 by ALTA.

Also go to http://www.alta.org and then see the RESPA Update section on the homepage to read the Statement of Gregory M. Kosin, Chair Government Affairs Committee on behalf of the American Land Title Association, before the Committee on Small Business U.S. House of Representatives, "RESPA Reform and the Economic Effects on Small Business," March 11, 2003.

The Federal Reserve Board Interpretation of Section 106 contains a restrictive view of tying and encourages "bundling" of services to individuals. See 68 Fed. Reg. 52024, 52034, Part VII. Coupled with HUD's proposal to allow bundling and tying under the guise of "guaranteed mortgage packages," the Board Interpretation allows financial institutions to mislead and overcharge consumers and harm competition in title services. For an excellent analysis of the HUD proposed Rule, see the Public Comment filed with the Department of Housing and Urban Development ("HUD"), by the American Land Title Association "ALTA Comment", October 4, 2002, in response to HUD's request for public comments on the proposed Rule on Real Estate Settlement Procedures Act (RESPA) Docket # FR 4727-P-01. Economic harm to the consumer may result from bundling bank products and aggressively cross-marketing non-bank products, because bundling bank products hides inflated fees, and cross-marketing assists large banks in cornering the market on non-bank products and driving up the fees

Individual loan seekers may be locked in by time restraints, and succumb to customer convenience, without realizing that they are receiving only one side of the picture- the Bank's side. An individual customer will not have time to investigate insurance products offered by competitive companies, to determine whether the bank's fees are too high. The Bank package itself becomes a form of non-disclosure to the consumer, because the consumer will believe that the package presents the total range of choices- the "complete picture"; and only the bank (the creditor) controls the information the borrower receives. Believing that the bank package is the complete picture, the borrower is seduced to choose the bank's package, rather than seeking lower prices for non-bank products.

Congressional action is required to re-define "anti-tying transactions," if implicit "bank coercion" of the customer to purchase non-bank products is to be permissible, contrary to original statutory purpose and legislative intent underlying the Bank Holding Company Act. The Federal Reserve Board does not have the authority to change court interpretation of Section 106.

Similarly, congressional action is required to add an exemption under RESPA for lender control of settlement services. HUD does not have current statutory authority to exercise its rule-making power to favor one group (namely lenders) over another (settlement service companies and title insurance companies). For an excellent analysis, see the ALTA Comment, October 4, 2002, (Id.). As of September 30th, 2003, HUD has not finalized the proposed Rule.

The ALTA Comment (Id.) explains the necessity for Congress to act to clarify the application of section 8 to certain payments or classes of payments; and explains why HUD has no authority to change the regulatory regime enacted by Congress. The rule proposed by HUD defeats the purpose of RESPA by setting up one Guaranteed Mortgage Package stating the total loan cost including settlement services such as title insurance without disclosing individual charges. The proposed HUD Rule exempts lenders from disclosing information on the individual services that may be contained in the package.

The Federal Reserve Board's Interpretation offers a restrictive view of tying and encourages "bundling," and HUD's proposal allows bundling and tying under the guise of "guaranteed mortgage packages." The Federal Reserve Board Interpretation and the HUD proposed rule to simplify mortgages dovetail to allow financial institutions to mislead and overcharge consumers and harms competition in title services.

Congressional action is required to add exemptions from the Real Estate Settlement and Procedures Act (12 U.S.C. 2601 et seq). HUD rule-making authority is insufficient to support a new exception to RESPA to exempt national banks offering a Guaranteed Mortgage Package created under the proposed RESPA reform rule from violating Section 8(c) of RESPA.

Congressional action is required to provide sufficient statutory authority to support the expanded exemptions from the anti-tying restrictions created by the Federal Reserve Board Interpretation of Section 106 of the Bank Holding Company Act Amendments of 1970 and related supervisory guidance (12 U.S.C. Sec. 19172(1)). The Board's proposed interpretation is impermissible under current law. The interpretation does not comport with the language, purpose, or legislative history of section 106.

Stewart Title appreciates the Federal Reserve Board's consideration of our comments. Please contact us if you have any questions about this filing.

Respectfully submitted,

Marietta M. Maxfield
Vice President/Special Counsel
Stewart Title Guaranty Company