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September 30, 2003

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Via Email: regs.comments@federalreserve.gov

RE: Docket No. OP-1158

Ladies & Gentlemen:

The Association of the Bar of the City of New York ("ABCNY" or the "Association")[1] welcomes the opportunity to comment, based on the recommendations of its Committee on Banking Law, on the proposed interpretation and supervisory guidance (the "Interpretation") issued by the Board of Governors of the Federal Reserve System (the "Board") on the Anti-Tying Restrictions of Section 106 of the Banking Holding Company Act Amendments of 1970 (the "Anti-Tying Restrictions" or "Section 106").

We are pleased that the Board has decided to publish interpretive guidance on a subject of great importance to the banking and financial services industry, one that has recently been the focus of increased attention on the part of various legislative and regulatory bodies. As ABCNY has previously observed, the concept of the Anti-Tying Restrictions is often

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1 The Association is one of the oldest and largest local bar associations in the United States, with a current membership of over 22,000 lawyers. The Association serves not only as a professional association, but also a leader and advocate in the legal community on a local, state, national and international level. The Association pursues its advocacy role through the work of over 170 committees, each devoted to a substantive area of the law. Among other activities, the Association's committees prepare comments for legislative bodies and regulatory agencies on pending and existing laws and regulations that have broad legal, regulatory or policy implications. Further information regarding the Association can be found at the Association's website, www.abcny.org.

misunderstood and misconstrued.[2] The Association believes that the Board, with its many years of experience in interpreting and enforcing the Anti-Tying Restrictions, should be the sole issuer of definitive guidance on Section 106, through the Interpretation. Moreover, the Association is also pleased that the Board addresses in the proposed Interpretation several of the concepts discussed in the Association's May 8, 2001 to the Board ("2001 Letter"), a copy of which is enclosed, in which we recommended that the Board consider exempting, by regulation, certain large commercial loan transactions and arrangements in the "wholesale" banking business.

The Association appreciates the Board's comprehensive and thoughtful analysis of Section 106 and, for the most part, concurs with the Board's stated conclusions regarding the interpretation of Section 106. We believe the "Question and Answer" format, and the inclusion of specific examples of common situations that arise under Section 106 and the Board's analysis of them, are well-done and will provide extremely helpful guidance to both banking organizations and supervisors as they attempt to navigate the legal and regulatory challenges of the post-Gramm-Leach-Bliley world of integrated financial services.

More specifically, the Association respectfully submits the following comments and recommendations regarding the proposed Interpretation.

Lending and Derivative Products

In Section III. A. of the proposed Interpretation, the Board specifically requests comment on how interest rate swaps, foreign exchange swaps, and other derivative products that are often connected with lending transactions should be treated under Section 106. The Association believes that when an interest rate or foreign exchange swap or other derivative product has been negotiated in connection with a proposed lending transaction for the purposes of mitigating the risks of extending credit to the relevant borrower, such derivative should be analyzed as an integral element of the loan transaction and not as a product in its own right. Derivatives transactions entered into between a bank and a customer in such circumstances should not be prohibited by the Anti-Tying Restrictions.[3]

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[2] See the Association's comment letter to NASD dated October 21, 2002 regarding *Special Notice to Members 02-64, Prohibition of Certain Bank Tying Arrangements.* A copy of this letter is enclosed for your reference.

[3] In footnote 23 of the proposed Interpretation, the Board explains that "[a]s 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." Although there is certainly customer demand for derivatives apart from the area of loans, and although banks do provide certain lending products and transactions separately from derivatives products as a general matter, we agree with the Board that a determination of whether something is one or two products is a "highly fact-intensive inquiry that depends on the nature and the character of the products and markets involved." In certain factual circumstances and in certain transaction scenarios, ABCNY believes that lending and derivatives products can be viewed as one rather than two products.

For example, it may be more economically efficient (and, hence, less risky for the lender) for a borrower to agree to a particular fixed or floating interest rate on its loan, but then simultaneously negotiate an interest rate swap or cap pursuant to which the borrower can swap all or part of its fixed or variable interest rate risk on the loan to another interest rate basis or cap a floating exposure. Similar arrangements are often made in multi-currency loan facilities, where a borrower may swap and/or hedge certain currency conversion risks under a credit facility for other currency exposures. In such cases, the derivative may be as key a part of the risk profile of the lending transaction as the stated interest rate on the loan because it facilitates the management of the borrower's interest rate or currency risks. As a result, when a derivative is an integral part of a lending transaction, ABCNY believes that it is not inappropriate under Section 106 to view these transactions as "one product". This approach will enable banks to offer credit to customers on the most efficient and flexible basis possible.

ABCNY also respectfully recommends that the Board use its exemptive authority under Section 106 to clarify that all derivative products that are permissible for banks to engage in with customers are deemed to be "traditional bank products," even if a derivative product is not so much an integral part of a lending transaction so as to be treated as one product Banks are, and have been for years, some of the most important participants in the markets for certain derivatives products. For many banking organizations today, the offering to customers of derivatives such as interest rate and currency swaps is viewed as traditional a banking activity as the making of loans and the taking of deposits. Congress, in Section 206 of the Gramm-Leach-Bliley Act of 1999, explicitly recognizes certain types of swap agreements as "identified banking products." At a minimum, the Board should consider providing "traditional bank product" status to derivatives that qualify as "identified banking products."

Relationship Banking

The Association applauds the Board for recognizing the concept and permissibility of certain types of "relationship banking" arrangements in its discussion of Mixed-Product Arrangements in Section IV.A.2. of the proposed Interpretation. As the Association noted in its 2001 Letter, "relationship banking" is often demanded by customers of their banks. It would be a perverse result under Section 106, which was intended to prevent the abuse of a bank's economic power over its customers, if the bank was unable to ensure that its business relationship with the customer was profitable based on the package of relationship services. Therefore, the proposed Interpretation recognizes that banks can set internal "hurdle rates," or profitability targets, for particular customers or types of customers that can be met through the purchase of one or more products in a mixed-product arrangement.

However, according to the proposed Interpretation, such a mixed-product arrangement would be permissible under Section 106 if the customer would have "a meaningful option" to satisfy the "hurdle rate" solely through the purchase of one or more "traditional bank products" and not be required to take non-traditional bank products. Although we appreciate the Board's attempt to balance the permissibility of "relationship banking" with the policy rationale

underlying the prohibition against the tying of traditional and non-traditional bank products, ABCNY questions whether the "meaningful option" criterion will prove workable in practice, particularly when a bank will need to make that determination on a prospective basis.

Footnote 51 of the proposed Interpretation, in which the Board attempts to illustrate by an example the "meaningful option" criterion, helps illustrate the Association's concern with the implementation of this standard. Based on that example, would it be necessary for a bank to determine what other relationships a customer may have with other banks or financial institutions with respect to "traditional bank products," as well as the nature of the duration and pricing of such arrangements, in order to determine whether it is, in fact, providing the customer with a "meaningful option" to satisfy the hurdle rate solely through traditional banking products? The Association is concerned that this criterion could lead to examiners "second guessing" banks' actions in this area.

Against this backdrop and to provide clearer guidance to banks with respect to mixed-product arrangements, we respectfully recommend that the Interpretation address two additional points. First, we suggest that the Interpretation make clear that it is permissible under Section 106 for a bank to at least discuss its approach to relationship banking with a customer, even if it has not yet done a full mixed-product analysis, so long as the bank is not imposing any impermissible condition on any grant of credit. Second, it would be helpful if the Interpretation clarified that even in a case where a bank does not offer an array of traditional bank products that would constitute a permissible mixed-product arrangement under Section IV. A. 2., it is permissible for a bank to cease providing credit to a customer if (1) the loan was not tied to another product when extended and (2) the relationship has not met the bank's "hurdle rate" as a result of voluntary use by the customer of other products and services (whether traditional or non-traditional).

"Wholesale" Banking Exemptions

Finally, the Association would like to reiterate and update the recommendations contained in its 2001 Letter that the Board exempt from the Anti-Tying Restrictions certain types of transactions in "wholesale" banking arrangements where the policy objectives of Section 106 are not adversely impacted. In its 2001 Letter, the Association proposed that the minimum amount at which an extension of credit be conclusively presumed to be a wholesale transaction was $25 million. The Association now believes that a more appropriate minimum figure is $50 million. Therefore, the Association continues to recommend that the following extensions of credit be exempted from Section 106, provided that the amount of each such extension of credit is at least $50 million:

a) Bridge loans made in anticipation of a securities offering the proceeds of which will be used to retire the bridge loans;

b) Syndicated loans made to institutional or corporate borrowers by a group of two or more lenders; and

c) Credit facilities used to back up or facilitate a company's non-banking funding programs, such as a commercial paper facility.

We leave to the discretion of the Board whether these recommended exemptions can be accommodated under the proposed Interpretation or would require further Board action.

* * * * * * * * * * *

Once again, the Association commends the Board for its thoughtful and timely action in proposing the Interpretation. We thank you for the opportunity to comment and appreciate your consideration of our recommendations. If you have any questions regarding this letter or wish to discuss our comments further, please contact the Chair of the ABCNY Committee on Banking Law, Bradley K. Sabel, at 212-848-8410, or Douglas Landy, Committee Secretary, at 212-848-8826.

Very truly yours,

Bradley K. Sabel
Chair, Committee on Banking Law

Enclosures

ABCNY COMMITTEE ON BANKING LAW MEMBERSHIP

Not all of the Committee members participated in the preparation of this letter, nor did the participation of a member mean that he or she supported the views expressed in this letter. Moreover, the Committee members acted only as individuals and not as representatives of the organizations to which they belong or by which they are employed, and therefore the views expressed in the letter are not to be considered the views of any governmental, commercial or private organization other than the Association.

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October 21, 2002

NASD
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Attn: Joseph E. Price
Director, Corporate Financing Department

Re: Special Notice to Members 02-64:
Prohibition of Certain Bank Tying Arrangements

Ladies and Gentlemen:

The Association of the Bar of the City of New York ("Association") welcomes the opportunity to comment on Special Notice to Members 02-64 ("Special Notice"). The Association is one of the oldest and largest local bar associations in the United States, with a current membership of over 22,000 lawyers. The Association serves not only as a professional association, but also as a leader and an advocate in the legal community on a local, state, national, and international level. The Association pursues its leadership role through the work of over 180 committees, each devoted to a substantive area of the law. Among other activities, the Association's committees prepare comment letters on regulatory developments where the issues involved have broad legal or policy implications. In that tradition, this letter, prepared by the Association's Committee on Banking Law, is offered for your consideration.

As an initial matter, we believe that the Special Notice has incorrectly cited the Association's letter dated May 8, 2001 to Ms. Jennifer Johnson, Secretary, Board of Governors of the Federal Reserve System, concerning Section 106 of the Bank Holding Company Act (the anti-tying provisions or "Section 106"). The Special Notice implies that the Association's letter supports the proposition that tying *by institutions subject to Section 106* commonly occurs in certain specified circumstances described in the letter (see footnote 6 of the Special Notice and accompanying text). As authors of the Association's letter, we assure you that no such notion was intended. Rather, the Association's letter recommended that the Federal Reserve adopt regulations *to permit* tying by parties subject to Section 106 under certain circumstances. As you are undoubtedly aware, there are NASD members engaged in commercial lending that do not have

regulated banking affiliates. Such parties are not subject to Section 106 and can, and we believe routinely do, tie commercial loans to investment banking services.

The Association's view as set forth in the May 8, 2001 letter is, and continues to be, that tying should be allowed when a bank product and an investment banking service are integral parts of the same transaction or series of related transactions, such as when a bridge loan is made to provide interim financing in anticipation of an underwritten bond offering, the proceeds of which will be used to repay the bridge loan. (Indeed, under some circumstances, a tie between a loan and the "take out" of that loan would not constitute a prohibited tie even under current law, although a specific regulatory interpretation in this regard would add much needed clarification.) In addition, the Association believes that tying should be permitted when there is no opportunity for banks to act in an anti-competitive manner, as in the case of syndicated loans where a number of banks are participating in the extension of credit.

The Association sent its May 8, 2001 letter to Federal Reserve in the belief that the tying prohibition, which dates back to the early 1970's, should be applied today in a manner that takes into account the dramatic changes that have occurred over the past thirty years in the financial services industry. The *bank* anti-tying statute, unlike the other antitrust laws, does not require any proof of competitive harm to be triggered. As the Association's May 8, 2001 letter points out, the public policy underpinnings of the bank anti-tying statute appears questionable at least in the context of "wholesale" transactions. We note that the Federal Reserve has expressly determined to implement the statute as it is written and, specifically, not to apply it to tying of products and services by non-bank affiliates of a bank, provided that no tying of bank products is involved. The Special Notice does not recognize this distinction.

Turning to the substance of the Special Notice itself, the Association feels that it is inconsistent with policy of functional regulation endorsed by the Gramm-Leach –Bliley Act of 1999, as it would seem to have a national self-regulatory securities organization interpreting and applying complicated bank regulatory provisions that have a long history of interpretation and application by the Federal bank regulatory authorities, and would duplicate on-going targeted inquiries currently underway by the Federal banking agencies. In general, we question the need for the Special Notice.

We understand that following issuance of the Special Notice, the NASD staff sent enforcement inquiry letters to financial holding companies with NASD member affiliates seeking the information on transactions where the NASD member rendered underwriting or investment banking services to a customer that maintained a commercial banking relationship with such member's banking affiliate, notwithstanding that there appears to be no evidence of a violation. This at a minimum suggests that NASD intends to examine the conduct of broker-dealers, even in the absence of any findings by a bank regulator of tying, to determine if they have aided and abetted violations of the tying prohibition by affiliated banks. If this is correct, the implications are quite troubling because the banking regulators have a long history of interpreting and applying the anti-tying provisions and the NASD could easily arrive at different interpretations of the same statutory prohibition. Contrary to the oversimplified analysis of tying that appears in the popular media, the application of the prohibition against tying to specific circumstances is complicated. It is therefore best left to interpretation and examination by banking regulators who have the necessary experience and expertise.

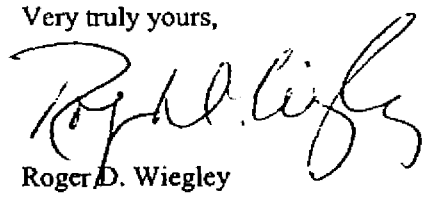
Further, the Special Notice and related inquiry letters are duplicative of targeted bank tying reviews by the Federal agencies. As you are undoubtedly aware, in response to inquiries of Representative Dingell related to press reports of alleged bank tying, the Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency have initiated a special targeted review of the tying issue at several of the country's largest banks and the General Accounting Office has undertaken to updated its May 1997 report "Bank Oversight; Few Cases of Typing have Been Detected." Accordingly, the Special Notice

and inquiry letters would seemly be covering the same ground currently under special review by the Federal agencies which have specialized expertise of long standing with the bank anti-tying provisions.

The Association acknowledges the general principle that in appropriate circumstances a broker-dealer's aiding and abetting of a material violation of certain laws might also be considered to be a violation of the NASD's rules. However, it is quite another matter to say that whenever a broker-dealer has aided and abetted a violation of a law imposed on an affiliate of the broker-dealer by the affiliate's regulator, that the NASD can assert jurisdiction over such activity. This, we believe, is beyond the scope of the NASD's authority. We respectfully submit that if the NASD is indeed by the Special Notice asserting such jurisdiction and claiming that aiding and abetting a violation of laws promulgated by other regulatory authorities is a violation of NASD Rule 2210 by not conforming with "just and equitable principles of trade", this seems to be a significant enough regulatory and policy change that it should be addressed through administrative procedures of the rule-making process, which includes filing such a rule change with the Securities and Exchange Commission and allowing for a public comment period thereafter.

At the very least, the Association recommends that any future notices issued by the NASD which involve Federal banking regulations be more closely coordinated with bank regulators to ensure that there is no risk of inconsistent application of such banking regulations. Bank Holding Companies which own both commercial banks and securities affiliates already face a complex regulatory web that is sometimes inefficient, redundant and confusing. As the banking and securities (and now insurance) industries evolve by developing products and services with characteristics similar to those offered by the competing industries, the overlap of jurisdiction of different regulators becomes greater and greater. This overlap can lead to inconsistent regulations (or interpretations of regulations) imposed by different regulators, with no means by which the affected financial institution can resolve the inconsistencies. Therefore, it is important that regulators exercise self-restraint and avoid asserting their authority over matters that are more appropriately left to the discretion of another regulator. The principle of functional regulation, which the Gramm-Leach-Bliley Act of 1999 affirms, make a compelling argument that those areas specifically within the province of one regulator should be left to thast regulator for primary interpretative and enforcement responsibility.

Very truly yours,



Roger D. Wiegley
Chair, Committee on Banking Law

Cc: Board of Governors of the Federal Reserve System
Office of the Controller of the Currency
General Accounting Office

Membership of the Committee on Banking Law

Not all the Committee members participated in the preparation of the letter nor did the participation of a member necessarily mean that he or she supported the views expressed in the letter. Moreover, the Committee members acted only as individuals and not as representatives of the organizations to which they belong or by which they are employed, and therefore the views expressed in the letter are not to be considered the views of any governmental, commercial or private organization other than the Association.

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May 8, 2001

Ms. Jennifer Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, N.W.
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Dear Ms. Johnson:

The Association of the Bar of the City of New York ("ABCNY" or the "Association") is one of the oldest and largest local bar associations in the United States, with a current membership of over 21,000 lawyers. ABCNY serves not only as a professional association, but also as a leader and advocate in the legal community on a local, state, national and international level. The Association pursues its advocacy role through the work of over 150 committees, each devoted to a substantive area of the law. Among their other activities, the Association's committees prepare comments for legislative bodies and regulatory agencies on pending and existing laws and regulations.

In that tradition, ABCNY respectfully recommends to the Federal Reserve Board that it consider exempting by regulation certain large commercial loans from the anti-tying provisions of Section 106 of the Bank Holding Company Act Amendments of 1970 ("Section 106"). This recommendation is based on the view of the ABCNY's Committee on Banking Law that the application of the anti-tying provisions to such loans in the current marketplace does not foster the purposes of Section 106, and, moreover, places institutions subject to Section 106 at a competitive disadvantage *vis-à-vis* their competitors not subject to Section 106. The Association believes that the proposal set forth in this letter is an appropriate subject for consideration by the Board.

Section 106 provides in relevant part that a bank may not "extend credit, lease or sell property of any kind, or furnish any service, or fix or vary the consideration for any of the foregoing, on the condition or requirement" that the customer (1) obtain or provide some additional credit, property or service from such bank other than a loan, discount, deposit or trust service, or (2) obtain or provide some additional credit, property or service from the parent bank holding company or its subsidiaries, other than as may be reasonably imposed by the bank in a credit transaction to assure the soundness of the credit.

Section 106 gives the Board the authority to grant exceptions to the prohibitions of Section 106:

> "The Board may by regulation or order permit such exceptions to the foregoing prohibitions and the prohibitions of section 4(c)(9) and 4(h)(2) of the Bank Holding Company Act of 1956 as it considers not to be contrary to the purposes of this section."

In Regulation Y the Board has extended the statutory exception which allows for tying of "traditional" bank products (loan, discount, deposit or trust service) within a bank to permit tying arrangements between banks and their affiliates, and has provided safe harbors for combined balance discounts and foreign transactions. Reg. Y, Section 225.7(b). The Association recommends that 12 C.F.R. Section 225.7(b) be amended to exempt from the tying restrictions the following extensions of credit: (i) bridge loans made in anticipation of a bond offering the proceeds of which will be used to retire the bridge loans; (ii) syndicated loans made to institutional or corporate borrowers by a group of two or more lenders, and (iii) credit facilities used to back up or facilitate a company's non-bank funding program, such as a commercial paper facility; provided, in each case, that the amount of the extension of credit is at least $25 million.

The legislative history of Section 106 shows that Congress enacted the anti-tying provisions of the Bank Holding Company Act "to provide specific statutory assurance that the use of economic power of a bank will not lead to a lessening of competition or unfair competitive practices." S.Rep. No. 1084, 91st Cong., 2nd Sess. 16, reprinted in 1970 U.S. Code Cong. & Admin. News 5519, 5535. Section 106 derives from Section 1 of the Sherman Act, 15 U.S.C. § 1, and Section 3 of the Clayton Act, 15 U.S.C. § 14. Under these federal antitrust statutes, a tying arrangement is illegal when there exist: (1) two separate products, (2) sufficient market power in the tying market to coerce purchases of the tied product, (3) involvement of a not insubstantial amount of interstate commerce in the tied market, and (4) anticompetitive effect in the tied market. Congress broadened Section 106 beyond the Sherman and Clayton Acts by dispensing with the need for proof of the economic power of banks (i.e., the seller) and proof of the anticompetitive effects of a tying arrangement in the tied

market. Congress also eliminated the need to prove the involvement of a not insubstantial amount of interstate commerce in the tied product.

The decision by Congress to restrict bank extensions of credit more stringently than transactions subject only to the provisions of the Sherman and Clayton Acts no doubt reflected the view that in the banking industry the power to coerce is inherent in the banking relationship and does not depend on an individual bank's market power. This may well be true in the case of individual retail and even small business customers of a bank, where the transaction costs associated with establishing or severing a banking relationship, as well as the loss of confidential financial data,can dissuade frequent changes and hence lend to the bank the kind of market power that Section 106 was designed to eliminate. *See*, Leonard, *Unfair Competition Under Section 106 of the Bank Holding Company Act*, 94 Banking L.J. 773, 787 (1977).

In the context of wholesale banking, however, the relevant factors are entirely different, particularly in light of today's credit markets. The banking industry has changed dramatically in the thirty years since the enactment of Section 106. In those three decades there has been a "sea change" in the business of banking from traditional loan products and deposittaking to a broad array of financial services. With regard to Section 106 and the recommendation contained in this letter, three recent developments arenoteworthy. First, short-term "bridge loans" made in anticipation of bond offerings, the proceeds of which will be used to repay the bridge loans, are now commonly used by corporations and LBO funds to finance acquisitions. Second, large credit facilities, typically involving loan commitments in the hundreds of millions or billions of dollars, are routinely syndicated among a number of participating financial institutions. And third, it is common today for large corporations to meet a significant portion of their capital needs through the commercial paper and debt capital markets.

In the case of a bridge loan that will be repaid with the proceeds of a bond offering, the lender has an obvious interest in ensuring that the bond offering is successfullycompleted. When the lender has a securities affiliate, as is frequently the case, the lender can determine at the time of entering into the bridge loan whether its securities affiliate can sell the bonds in an underwritten public offering or private placement. A lender *cannot* always have the same confidence that an unaffiliated securities firm will be able to successfully sell the bonds. Yet if the bonds are not sold, the lender may be left holding a short-term loan that has gone into default. Hence, it is a typical expectation of borrowers and other market participants that the bridge lender or one of its affiliates will be the lead manager in a "take out" bond offering. This expectation, while relied upon by lenders that are subject to Section 106, is not a certainty and cannot be included in the parties' formal agreement because of the tying prohibition.

In contrast, bridge lenders that are not subject to Section 106 routinely ask for an explicit agreement from the borrower to the effect that the lender or one its affiliates will be appointed as the lead manager for the bond offering or, alternatively, if the borrower chooses a different financial institution to lead the bond offering, requiring the borrower to pay a substantial "exit fee" to the bridge lender.

Syndicated loans present another situation where Section 106 no longer serves its intended purpose. Lending institutions are often asked by corporate borrowers and LBO funds to compete for the role of syndication agent or arranger on a large credit facility by offering indicative terms for the facility. Similarly, after the syndication agent or arranger is chosen, lenders with a pre existing relationship with the borrower are often asked by the borrower (or by the agent or arranger on behalf of the borrower) to participate in the credit facility. Competition among lending institutions for the role of agent or arranger in a syndicated credit is often intense. Section 106 is not needed to reduce anti-competitive pressures. Indeed, it would actually *increase* the competition among lenders if all lenders, not just those outside the reach of Section 106, could offer more favorable terms on the credit facility, such as reduced arranger or agent fees, that were conditioned upon the borrower's a greement to provide future investment banking business to the lender.

When a lending institution is asked by a borrower to participate in a syndicated credit facility because the borrower wants all of its "relationship banks" to participate, the lending institution may find the opportunity unattractive from a business perspective but may feel compelled to participate simply to preserve its good relationship with the borrower. It would not violate the intent of Section 106 to allow lending institutions to bargain for other business as a *quid pro quo* for participating in the credit facility. Such bargaining would, of course, be subject to the constraints imposed by Sections 23A and 23B of the Federal Reserve Act, *i.e.*, a bank lender could not extend credit at a below-market rate in order to provide an indirect benefit to an affiliated broker-dealer.

The third significant development since the enactment of Section 106 has been the increasing reliance by large corporations on the commercial paper and public debt markets to raise capital. Bank credit facilities are in many instances used by corporate borrowers only as a back-stop to ensure liquidity in the event of disruptions in the commercial paper market or to provide funding for short term exigencies that exceed the company's commercial paper limits. From the banks' perspective, however, these credit facilities, often consisting of undrawn loan commitments, are not themselves an attractive use of capital, but instead are viewed as part of a multi-service relationship with the borrower. Allowing banks to negotiate a lower fee for back-up credit facilities in return for capital-markets related services would not only provide a benefit to the borrowers but also give recognition to the fact that bank debt and capital markets debt are typically

integrated in a corporation's borrowing strategy. Again, such "package pricing" would be subject to Sections 23A and 23B.

The ABCNY respectfully submits that the purpose of Section 106 is not served by restricting the ability of banks to bargain for investment banking services in connection with the extension of credit in the foregoing situations. The Association therefore suggests that 12 C.F.R. § 225.7(b) be amended to add a fourth safe harbor for transactions in which credit in an amount in excess of $25 million is offeredand one or more of the following circumstances is applicable: (1) the extension or terms of such credit is conditioned on the requirement that the borrower obtain capital markets related services from the lender or an affiliate of the lender which are designed to facilitate or effectuate the repayment of the credit in accordance with its terms, (2) the credit is or is expected to be part of a multi-bank loan facility in which two or more unaffiliated banks are expected to have participations of at least $25 million in the aggregate, or (3) the borrower has previously obtained or expects to obtain financing through the issuance of debt securities or commercial paper, the extension of credit is designed to support, facilitate or provide a back-up for the borrower's non -bank funding program, and the extension of credit or terms thereof are offered on the condition that the borrower obtain from the lender or an affiliate of the lender services relating to the raising of capital through the public or private securities markets. We note that if this proposed safe harbor were to result in any anticompetitive practices, the Board could disallow further reliance on the exemption pursuant to paragraph (c) of 12 C.F.R. 225.7.

As further support for the recommendation in this letter, we would like to add that passage of the Gramm-Leach-Bliley Act ("GLB") had as one of its purposes making financial holding companies full competitors in the marketplace for financial services. Financial holding companies are in direct competition with major investment banking firms and commercial finance companies not subject to Section 106 and, as noted above, it has become a common practice for the providers of financial services not subject to Section 106 to require a borrower, as a condition to the extension of credit to such borrower, to use the same credit provider or one its affiliates for investment banking services in other transactions. Without an exemption such as the one recommended above, institutions subject to Section 106 engaged in investment banking activities are at a significant competitive disadvantage to institutions which are not so constrained.

The proposed exemption will not affect the provision of retail or small business banking products. By limiting the exemption to extensions of credit where the amount of the credit is $25 million or more, only large corporate and institutional borrowers will be affected, and such borrowers have the financial sophistication to bargain for credit on a stand-alone basis or to negotiate a favorable fee arrangement for credit tied to other services, just as they do now when they deal with financial firms that are not subject to Section 106.

In some respects, an exemption from the prohibitions of Section 106 for large corporate loans would be analogous to the common exemption from State usury laws for large loans. Usury laws protect retail consumers against excessive interest rates that banks, using the "power to coercce" that is presumed to be inherent in the retail banking relationship, might otherwise be able to charge. However, there is typically an exemption for loans above a specified amount. For example, New York has a statute, General Obligation Laws § 5-501.6, which exempts from the State's usury law all loans of $2,500,000 or more. Such exemptions reflect the legislative judgment that borrowers of amounts over $2,500,000 possess the sophistication and bargaining power to resist anticompetitive pressures and do not need statutory protection.

Similarly, we do not believe that the proposed exemption will have an adverse effect on small businesses because of the $25 million threshold. Using data found in the 1993 National Survey of Small Business Finances sponsored by the Board of Governors and the Small Business Administration (the "Survey"), the following table shows the amount of line of credit commitments and outstanding loan balances for equipment, motor vehicle, commercial mortgage and other loans as of fiscal year-end 1993 for the wide variety of small businesses[1] covered in the Survey:

Amount	Percent
Less than $1 million	97.8
$1 million to <$5 million	1.9
$5 million to <$10 million	0.2
$10 million to <$15 million	0.1
$15 million to <$20 million	0.0
$20 million to <$25 million	0.0
Greater than $25 million	0.0

The table shows that the overwhelming majority of loans to small businesses were below $5 million, with scarcely any loans above $10 million. While the table shows outstanding loan balances, not the original loan amount – which would be higher – the proposed $25 million threshold is so far above the amount of loans that the small businesses in the Survey had outstanding that it seems clear that small businesses would not be affected by the proposed exemption.

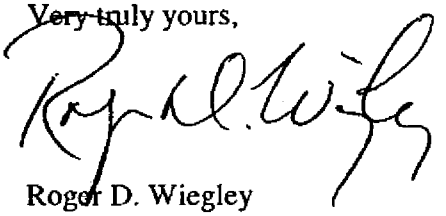
[1] The Survey measured business size in three ways: by average number of full-time equivalent employees (up to 499); 1993 sales; and year-end 1993 assets. Most of the firms surveyed were at the lower end of these ranges: nearly 70 percent had fewer than five full-time equivalent employees, and fewer than one in twenty had more than $5 million in assets or sales. See generally Financial Services Used by Small Businesses: Evidence from the 1993 National Survey of Small Business Finances, 81 Federal Reserve Bulletin 629 (1995).

seems clear that small businesses would not be affected by the proposed exemption.

For the reasons discussed above, the Association believes that an exemption from Section 106 for large corporate loans would actually benefit borrowers, rather than disadvantage them, by increasing competition through pricing negotiations that contemplate a combination of both credit and investment banking services, and it would also create parity between multi-service financial institutions subject to Section 106 and those not subject to Section 106 in terms of competition for investment banking services.

Thank you for considering this recommendation.

Very truly yours,



Roger D. Wiegley
Chair, Committee on
Banking Law

Attachment: Membership of Committee on Banking Law

cc: J. Virgil Mattingly, Esq.
Scott G. Alvarez, Esq.

ABCNY COMMITTEE ON BANKING LAW MEMBERSHIP

Individuals named below who are employed by Federal or State governmental agencies or self-regulatory organizations have abstained from and do not express any opinion on the issues and recommendations in the foregoing letter.

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