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May 3, 2004

Via email to comments@fdic.gov

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429.

Re: RIN 3064–AC78; FDIC Proposed Implementation of Regulation W's Limitations on Transactions with Affiliates for State Nonmember Banks: 12 CFR Parts 303 and 324; 69 Federal Register 12571; March 17, 2004

Dear Sir or Madam:

Sections 23A and 23B of the Federal Reserve Act place restrictions on transactions with affiliates for reserve member banks. Section 18(j)(1) of the Federal Deposit Insurance Act (FDI Act) provides that Sections 23A and 23B "shall apply with respect to every nonmember insured bank in the same manner and to the same extent as if the nonmember insured bank were a member bank." In December of 2002, the Federal Reserve Board (FRB) published a final rule implementing these sections of the Federal Reserve Act: Regulation W at 12 CFR 223. The Federal Deposit Insurance Corporation (FDIC) now is proposing to adopt a regulation applying to state nonmember banks that largely follows Regulation W, but with important differences. The American Bankers Association (ABA) brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership - which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks - makes ABA the largest banking trade association in the country.

Background

The FDIC is proposing to add 12 CFR Part 324 to make clear that insured state nonmember banks must comply with the restrictions and limitations contained in Regulation W in order to comply with sections 23A and 23B of the Federal Reserve Act and section 18(j)(1) of the FDI Act. New Part 324 will expressly incorporate through cross reference the substantive provisions of Regulation W but will identify the FDIC as the appropriate agency for state nonmember banks in the administration and interpretation of those requirements and in granting exemption requests. Section 324.5 provides that insured state nonmember banks may obtain an exemption from the restrictions and limitations of this part concerning section 23A if the FDIC determines that such an exemption is in the public interest and is

consistent with the purposes of section 23A. Procedures for filing exemption requests are proposed in this section and would, if adopted, be added to part 303 of FDIC's regulations. Finally, Section 324.6 provides that determinations that a shareholder or company exercises a controlling influence over another company will only be made after notice and opportunity for hearing.

ABA Position

ABA supported the FRB's adoption of Regulation W, believing that the regulation made understanding of and compliance with Sections 23A and 23B easier. Therefore, we in general support the FDIC's virtual uniform adoption of Regulation W in the FDIC's Part 324. However, the FDIC poses some difficult issues in its adoption, because the FDIC interprets its statute as giving the FDIC authority to independently apply Sections 23A and 23B to state nonmember banks, and the FDIC specifically is adopting certain exemptions for affiliates under Section 24 of the FDI Act that the FRB has already indicated it probably would not adopt. Section 24 subsidiaries (and thus affiliates under Sections 23A and 23B) engage in activities approved by the FDIC but not authorized for national banks or state member banks. The FDIC highlights these issues in its proposal and asks whether the FDIC's approach is correct or beneficial. While this is a difficult question, ABA has concluded that it is appropriate to support the FDIC's approach to implementing the restrictions of Sections 23A and 23B.

We note that the General Counsel of the Federal Reserve Board, Virgil Mattingly, in a letter dated February 6, 2004, disputes the FDIC's authority to adopt anything different than the FRB has provided in Regulation W. Mr. Mattingly points out that the FDIC is not granted explicit authority to make such exemptions, while he reads the statute as expressly authorizing the FRB to make regulations and grant exemptions under these sections of law. He further argues that Congress did grant to the Office of Thrift Supervision authority to add additional restrictions on federal savings associations but not to grant any exemptions, which suggests to him that Congress would not have intended the FDIC to have exemptive authority for nonmember banks. The FDIC in its comments to the FRB on the proposed Regulation W in a letter dated August 15, 2001, argues that positioning the FRB as the sole interpreter of Sections 23A and 23B would undermine the FDIC's authority to regulate state nonmember banks, such as in making determinations that a control situation existed that needed supervisory application of the restrictions on transactions with affiliates. The FDIC further argues that amendments in the Gramm-Leach-Bliley Act adding Section 46 of the FDI Act specifically provided that only subsidiaries acting as "principal" were affiliates for purposes of Sections 23A and 23B. That result is contradicted by the reading of the FRB, which would make subsidiaries under Section 24 of the FDI Act - as well as subsidiaries acting as "agent" - affiliates for purposes of Sections 23A and 23B.

ABA believes that the various statutory provisions discussed above are not entirely clear as to whether the FRB is the sole exemptive and interpretative authority under Sections 23A and 23B for state nonmember banks. At the same time, ABA believes that an overriding principle of our banking structure consistently supported by the Congress has been the maintenance of a viable dual banking system. Congress' commitment to a dual banking system is seen in the authority granted to the FDIC under Sections 24 and 46 of the FDI Act with respect to subsidiaries of state nonmember banks engaging in activities not authorized for national banks and state member banks, all of which are members of the Federal Reserve System. ABA concludes that the FRB's approach in fact would weaken the dual banking system unduly and unnecessarily, while the FDIC's approach comes closest to reconciling Congress' desire to ensure that banks are limited in their transactions with affiliates while at the same time maintaining and supporting the dual banking system. We conclude that

adoption of the FRB's position that it is the sole exemptive authority under the these statutes and that it is not appropriate to exempt Section 24 subsidiaries would greatly undermine the viability of these subsidiaries conducting activities authorized for state banks but not for national banks. This in turn would be a hard blow directly against one of the fundamental concepts of the dual banking system - that the several states serve as laboratories to explore and develop new powers and authorities for banks, which if successful are then likely to be adopted by the Congress for national banks. Thus, ABA concludes that the FDIC should adopt its regulation as proposed.

From this point, ABA makes these additional comments on the FDIC's proposal:

> ABA does not believe that the FDIC should set out the text of Regulation W in full in its own regulation. Consistency between the regulators seems best served by the FDIC's approach of adopting the text of Regulation W by reference.
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> The FDIC should direct state nonmember banks to file exemptive requests with the FDIC rather than with the FRB; however, the FDIC and the FRB should continue their close consultation on such requests.
>
> ABA believes that the procedures for exemptive requests are sufficient and, further, supports the FDIC's adopting specific time periods for acting upon such requests, subject to the provision that the FDIC has received a complete application for an exemption, including any additional information that the FDIC might require in order to make an exemption determination.
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> ABA does not support delegating the exercise of exemptive authority, given that there is conflict between the FRB and the FDIC as to whether the FDIC has the authority in the first place. ABA recommends that the FDIC Board consider and decide exemptive requests.
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> ABA believes that the issue of a control determination most often arises in the field during examination and action may well need to be taken immediately. Therefore ABA recommends that control determinations be delegated, but that such determinations be appealable to the Board (but not subject to suspensive appeal).
>
> ABA believes that the FDIC is correct that the proposed exemption for Section 24 subsidiaries that were established prior to the publication of this proposal from Part 324 will not adversely impact the public or be inconsistent with the purposes of section 23A and 23B.
>
> ABA does not recommend enlarging the subsidiary exemptions at this time and offers no requests for additional exemptions.
>
> ABA supports a phase-in period from the date of adoption of the final regulation, and believes that the three-month phase-in adopted by the FRB in their final regulation should be adequate.

In conclusion, ABA recognizes that there is a serious and considered difference of opinion between the FDIC and the FRB on whether the FDIC has the authority to adopt the proposal as issued. ABA believes that the FDIC's approach is compatible with the statutes considered and is more harmonious with the maintenance of the dual banking system, but ABA does not want state nonmember banks to suffer from the fallout from a serious disagreement between regulators. ABA urges the FDIC and the FRB to explore any mechanisms available to them to obtain a definitive interpretation of these statutes so as to end any conflict between them. If either the FDIC or the FRB has questions about this comment letter, please call the undersigned.

Sincerely,

Paul Smith
Senior Counsel