

MEMO# 10688

February 2, 1999

HOUSE BANKING CHAIRMAN LEACH INTRODUCES FINANCIAL MODERNIZATION BILL; HOUSE AND SENATE SCHEDULE ACTION

1 See Memorandum to the Board of Governors No. 60-98, Federal Legislation Members No. 23-98, Primary Contacts Member Complex No. 80-98, and Public Information Committee No. 41-98, dated September 24, 1998. [10688] February 2, 1999 TO: BOARD OF GOVERNORS No. 5-99 FEDERAL LEGISLATION MEMBERS No. 3-99 PRIMARY CONTACTS - MEMBER COMPLEX No. 7-99 PUBLIC INFORMATION COMMITTEE No. 2-99 RE: HOUSE BANKING CHAIRMAN LEACH INTRODUCES FINANCIAL MODERNIZATION BILL; HOUSE AND SENATE SCHEDULE ACTION

House
Banking Committee Chairman James Leach (R-IA) introduced H.R. 10 "The Financial Services Act of 1999" on January 6, the opening day of Congress. Chairman Leach subsequently announced a schedule of mid-February hearings on the bill, and targeted late February or March for committee action on the measure. The Institute has been invited to testify on February 10. The House Commerce Committee, which will also consider H.R. 10, has not yet announced its schedule. Also in mid-January, Senate Banking Committee Chairman Phil Gramm (R-TX) announced that the first priority of the Senate Banking Committee would be to report a financial modernization bill; he tentatively scheduled committee action on a modernization bill for February 25. Chairman Gramm does not intend to introduce a bill before the hearings, but will instead work from a staff draft. Generally speaking, H.R. 10 reflects the legislation that the Senate was expected to approve last year.¹ Holding Company Activities and Regulation H.R. 10 would repeal the Glass-Steagall Act's provisions that restrict bank and securities firm affiliations within a bank holding company system. It would also amend the Bank Holding Company Act to permit affiliations among financial services companies, including banks, registered investment companies, securities firms and insurance companies. The Federal Reserve Board (FRB) would be designated the "umbrella" regulator of both bank holding companies (BHCs) and the new financial services holding companies (FSHCs). Under the legislation, the authority of the FRB when exercising its general supervisory authority to regulate, examine or take enforcement action against regulated, non-bank subsidiaries of the holding company such as investment advisers, broker/dealers and insurance companies is carefully limited. The exception to this limitation would be a determination by the FRB that actions by a regulated subsidiary within the holding company pose a material risk to an affiliated bank or the domestic or international payments system. The current H.R. 10 places the same limitations that apply to the FRB on the general supervisory authority of the FDIC. It

does not currently extend the same limitations to the Office of the Comptroller of the Currency or the Office of Thrift Supervision. Community Reinvestment Act H.R. 10 contains no provisions to extend the Community Reinvestment Act to investment companies or other non-bank entities. Commercial Affiliations H.R. 10 restricts commercial affiliations for financial services holding companies. Only a limited amount of those non-financial activities that were conducted upon application to become a FSHC would be permitted, and those must be divested within 10-15 years. In a recent speech in Washington, Chairman Leach reiterated his strong opposition to mixing banking and commercial activities. He stated "[n]o one should misunderstand the depth of my opposition to mixing banking and commerce or any so-called basket approaches. I cannot in good conscience send a bill to the President which would jeopardize the taxpayers and do more harm than good to the U.S. economy." Unitary Savings and Loan Holding Companies Under existing law, without activity restrictions, any commercial company may control a single thrift, as a unitary savings and loan holding company (USLHC). However, H.R. 10 would change that by barring any company engaged in commercial or nonfinancial activities from owning a thrift. Any commercial company that was a USLHC or applied to control a unitary thrift before October 7, 1998, would be allowed to continue operations under a limited grandfather provision. However, a grandfathered USLHC would only be allowed to sell its thrift operation to another grandfathered USLHC or to a financial company. Bank Securities Activities H.R. 10 amends the various exemptions for banks and their activities under the Investment Company and Investment Advisers Acts of 1940 and the Securities Exchange Act of 1934. Thus, certain bank activities that were previously exempt would now be required to be conducted in a broker-dealer. Also, a bank or its separately identifiable division that advises an investment company would be required to register as an investment adviser. We will keep you informed of further developments. Matthew P. Fink President