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Robert Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Transmitted via email to comments@fdic.gov

Dear Mr. Feldman:

The Securities Industry Association ("SIA") appreciates the opportunity to respond to the questions recently issued by the FDIC for public comment regarding industrial loan corporations. [1]

SIA members have a vital interest in the proper regulation of industrial loan corporations (now more properly referred to as "industrial banks"). Most of the largest and leading securities companies in the nation have bank subsidiaries and most of those are industrial banks. Industrial banks owned by SIA members hold over $95 billion in assets, which is the majority of all assets in the ILC industry. SIA members also own some of the largest and oldest industrial banks.

Industrial banks generally, and SIA member owned banks in particular, have established a record of safety and financial strength comparable to any group of banks that ever existed. No SIA member owned bank has failed. Capital ratios and profitability are significantly higher than the average for banks generally. All SIA member owned industrial banks are based in Utah and every Utah based industrial bank has a CRA rating of satisfactory or outstanding. In the history of the industry, no significant problem has arisen that needs to be fixed or that would warrant any additional restrictions or prohibitions on industrial banks generally or any particular group of banks.

The banks owned by SIA members are critically important to meet their customer's financial needs. SIA will strongly oppose any unnecessary, unjustified or politically motivated restrictions on these banks.

To the largest extent, the development of SIA member owned banks is the result of the same market forces that prompted Congress to repeal the Glass-Steagall Act in 1999.

In 1987 the FDIC published a study titled <u>*Mandate for Change*</u> that examined the role of banks in the developing financial services markets and the need for laws separating banking from securities and commerce. Among other things, it reviewed the role of bank loans and companies offering both banking

[1] SIA is a national trade association that brings together the shared interests of more than 600 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals and its personnel manage the accounts of nearly 93 million investors directly and indirectly through corporate, thrift and pension plans. In 2005, the industry generated an estimated $322.4 billion in domestic revenue and an estimated $474 billion in global revenues. (More information about SIA is available at: www.sia.com.)

and securities services in the stock market crash and the Great Depression. It found that the reasons for enacting the Glass-Steagall Act, which separated the banking and securities industries, were unfounded and the Act had become counterproductive in the modern financial services market. It also examined the separation of banking and commerce and found that policy, as embodied in the activities restrictions in the Bank Holding Company Act, was unjustified and in conflict with the needs of the financial services market. The study ended by advocating repeal of both the Glass Steagall Act separating banks and securities and the Bank Holding Company Act separating banking and commerce.

This study acknowledged a growing market demand for a full range of products and services from customers of both banks and securities companies. Increasingly over the past twenty years, major securities and banking companies have faced growing demand to offer their customers securities underwriting, debt financing and transactional services from one source. Obtaining financial products and services from multiple companies is inefficient both in time and cost. For commercial customers, obtaining securities and loans from one source results in volume pricing and a more coordinated suite of products and services. Full service providers also tend to be more innovative. It is easier to design newer and more specialized products when the company has a broader range of expertise and does not have to worry whether a new product will qualify as one that institution can offer.

In 1987, Congress enacted the Competitive Equality Banking Act ("CEBA") which, among other things, exempted owners of industrial banks from the Bank Holding Company Act (except the anti-tying provisions). That enabled securities firms to respond to market demands for broader product and service offerings by organizing an industrial bank subsidiary. This is the legal authority chosen by most SIA members to organize a bank subsidiary to better serve their customer's needs.

Passage of the Gramm-Leach-Bliley Act ("GLBA") in 1999 gave securities companies the option to become a financial holding company regulated by the Federal Reserve but few made the switch from an industrial bank or selected a financial holding company structure when organizing new banks after the GLBA became law. Many securities firms were already successfully operating with industrial bank subsidiaries and saw no advantage in changing. Most securities companies organizing banks after the enactment of the GLBA selected an industrial bank and the "bank centric" regulatory model administered by the FDIC, which involves unified regulation of the bank and its affiliates by one regulator combined with measures to strengthen independent control of the bank. That model has worked well for other securities firms and is generally more efficient and logical than the bifurcated regulatory structure of a financial holding company. Many SIA member companies also noted that the standards and requirements applicable to a financial holding company are based on the regulation of traditional bank holding companies, which are substantially dissimilar to securities companies in terms of activities and financial structure. For that reason, most securities firms prefer to retain a structure where the Securities Exchange Commission ("SEC") is the consolidated regulator of the parent and its non bank affiliates.

It is not necessary for a SIA member with a bank subsidiary to become a financial holding company to be regulated by a "consolidated" regulator. Currently, all SIA members with industrial bank subsidiaries are subject to consolidated regulation of the parent holding company and affiliates by the SEC. The SEC's consolidated supervision program focuses on all the same areas of enterprise-wide risk as those of the Federal Reserve and the Office of Thrift Supervision ("OTS"). Like them, it is focused on the maintenance of a strong capital position based on the risk presented by the institution and on the implementation by the institution of robust risk management procedures. Like the bank regulators, its supervision focuses on the firm's ongoing risk management, rather than its position at any one moment in time. There are inevitable differences among agencies in their methods of supervision and the details of their supervisory programs. The United Kingdom's Financial Services Authority, the Federal Reserve, the OTS, the SEC and other regulators may differ in details of their approach, but those differences do not indicate that any of them is deficient or superior. However, no other U.S. regulator has the depth of experience and expertise in the securities business that the SEC has developed. It has a proven track record in overseeing securities firms and enforcing the laws applicable to them. While other agencies might be better suited to oversee firms engaged principally in commercial banking, no other agency is better positioned to provide effective oversight of a securities firm and its business.

For companies under consolidated regulation by the SEC, it makes no sense to add another consolidated regulator with duplicative jurisdiction over the parent and other affiliates under the principles of functional regulation adopted as part of the financial holding company structure in the Gramm-Leach-Bliley Act.

Bank subsidiaries have added significant value and versatility to SIA member corporate groups. Many SIA member owned banks hold idle funds swept from brokerage accounts as deposits. Brokerage customers have a clearly demonstrated preference for sweeping their funds into federally insured deposit accounts instead of uninsured money market mutual funds, which was the common practice in the past. This has provided a reliable and low cost source of deposits to fund traditional banking products and services offered to customers of the corporate group and to people and companies that have never dealt with a member of the corporate group in the past. Consumer and commercial loans have also proven to be very popular. In fact, many securities underwriting customers demand that the securities company provide loans and debt financing to take care of other financial needs. The most cost effective way to fund bank quality loans is with deposits. Applying traditional bank "hurdle rates" when customers obtain multiple products and services allows the securities company to offer its products and services at lower cost. This is a natural and logical way to develop a business and is necessary for many companies to retain their best customers. It is also critical for any company that competes internationally with companies based in other nations.

Most bank products and services are provided directly to third party customers and are comparable to a consumer or commercial loan provided by any other bank. Sections 23A and 23B of the Federal Reserve Act and the anti-tying laws are carefully followed when affiliate transactions occur.

With this background, we will now respond to the specific questions the FDIC issued for response.

1. *Have developments in the ILC industry in recent years altered the relative risk profile of ILCs compared to other depository institutions? What specific effects have there been on the ILC industry, safety and soundness, risks to the Deposit Insurance Fund, and other insured depository institutions? What modifications, if any, to its supervisory programs or regulations should the FDIC consider in light of the evolution of the ILC industry?*

The SIA and its members are aware of no changes or developments in the ILC industry, the regulatory system or the financial services markets that have increased the risk profile of industrial banks generally or those banks owned by securities firms. SIA member owned banks have consistently received the top ratings for safety, soundness and compliance, capital ratios have remained well above the average for banks generally, loss ratios are well with the range for healthy banks, and CRA ratings remain among the best in the nation. The industry has grown substantially during the past several years, mostly due to the growing market demand for the products and services provided by the industrial banks and the proven success of the FDIC's unified regulatory model.

SIA members are proud of the leading role they have played in developing and testing the unified system of regulation for industrial banks and their affiliates, which the FDIC designated the "bank centric" regulatory model. This model unifies regulation of the bank and its affiliates under the bank's regulators. It enables the bank's regulators to oversee all relationships and transactions between the bank and its affiliates. It also provides for uniform standards. When matters arise that involve both the bank and an affiliate, the regulators can examine the whole transaction or issue, not just the part involving the bank. Remedial actions or agreements can also be coordinated between the bank and affiliate.

The bank centric system is more efficient and logical than the bifurcated system used to regulate traditional bank holding companies and financial holding companies. Under the traditional system, holding companies and affiliates are regulated separately from the bank by the Federal Reserve under what are often different regulatory standards. If a bank examiner encounters a problem at the bank involving an affiliate, it must usually work through the Federal Reserve to address the issue with the affiliate. The Federal Reserve is not required to coordinate with the bank's regulators on either the timing or the actions taken to address problems involving both entities.

More importantly, the bank centric regulatory model is more compatible with the financial services markets than the outdated traditional bank holding company model. The traditional bank holding company model was designed to regulate a segregated, stand alone industry at a time when banks provided most credit in the economy and the Glass-Steagall Act required a complete separation of banking and securities companies. When the Bank Holding Company Act was passed, few companies wanted to own a bank because of geographic limitations and the cost of providing credit internally. As former Chairman Alan Greenspan noted, the traditional bank holding company model only works well if the bank is the primary asset of the group.

Since the Bank Holding Company Act was enacted, new technology and the repeal of most geographic restrictions on banks has enabled financial services to expand throughout the economy. Today, credit is an integral part of most businesses and companies outside the purview of the Bank Holding Company Act may now provide more credit than traditional banks. This development is driven by market demand. Because of this abundance of credit supplied by a broad and diverse group of companies, it is no longer necessary to segregate banks from all other businesses to ensure equal access to credit. The primary public policy consideration today is that a financial services business that would operate most efficiently and cost effectively with a bank subsidiary should have access to a bank charter. The bank centric model accommodates those companies and so serves public needs and convenience better than the traditional bank holding company model.

Another unique feature of the bank centric regulatory model is enhanced requirements to ensure that the bank operates independently under highly qualified boards and management. These requirements respond to the fact that an industrial bank can have broader affiliations than a bank controlled by a traditional bank holding company. Conflicts of interest are less likely in a traditional bank holding company group because there is often only the bank and a smaller and weaker holding company. To ensure the bank is protected when it is part of a much larger and diverse group, most industrial banks are required to have independent boards with a majority of outside directors. Directors are expected to have strong credentials in addition to independence such as prior experience as a banker, accountant, attorney representing banks, or regulator. Overlapping directors are less common than in a traditional bank, where interlocks are encouraged by the Federal Reserve. An industrial bank must have an audit committee composed entirely of outside directors which has sole authority to select auditors, schedule audits and receive audit reports. Management must be highly qualified, usually with a long history of successfully serving in similar positions prior to joining the bank.

The bank centric model has been tested for twenty years on a broad scale and under the normal stresses and cycles of the market and has proven safe and effective. The model has also been tested in more extreme circumstances (involving owners outside of the securities industry) and proven effective in averting bank failures. The record accumulated during this time demonstrates that industrial banks are generally safer, financially stronger, and less prone to failure than other kinds of banks. The record also highlights the higher level of support that most industrial banks receive from their parents and affiliates and the very real benefits that produces for the banks and the banking system.

SIA members are aware of no flaws or weaknesses in the bank centric model that would require an amendment of the law or additional restrictions on industrial banks generally or any segment of the industrial bank industry. Under that model, the banks' regulators have extensive authority over both the bank and its affiliates. SIA members are well aware that having a bank subsidiary subjects the securities companies and all of their affiliates to examinations by the banks' regulators, operational restrictions deemed necessary by the regulators to protect the bank, and the possibility of cease and desist orders, civil money penalties, and orders banning institution affiliated parties from control of any banking institution for life.

We note that the FDIC itself has consistently taken the position that it has all of the regulatory authority needed to oversee and supervise both the industrial banks and their affiliates. This position was first publicly stated in *Mandate for Change* in 1987 and strongly reaffirmed by the last chairman of the FDIC as recently as one year ago.

2. *Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based on whether the owner is a financial entity or a commercial entity? If so, how and why? Should the FDIC apply its supervisory or regulatory authority differently based upon whether the owner is a financial entity or a commercial entity? If so, how should the FDIC determine when an entity is "financial" and in what way should it apply its authority differently?*

SIA is aware of no significant difference in the risks presented by industrial banks relating to whether the bank's owner is a financial or a commercial company. SIA members that own industrial banks are all currently subject to consolidated regulation but we do not believe the lack of consolidated regulation of the holding company and non bank affiliates would expose the bank to greater risks.

It would be difficult to adopt bright line definitions of "financial" and "commercial" to distinguish parent companies for purposes of imposing different standards and restrictions on their subsidiary banks. The markets are too dynamic and innovative to accommodate static definitions. One of the primary strengths of the modern financial services market is the number of new products and services and investment opportunities emerging on a regular basis. New products and opportunities cannot be fully anticipated today and there is no reason to conclude that any new investment or activity undertaken by an affiliate that did not fall squarely into an outdated definition of "financial" would be inherently risky to a bank.

Any definition of "financial" or "commercial" will be unavoidably arbitrary. The risk is high that a definition will inadvertently affect financial services providers in the future by subjecting a company to a classification that will harm its banking subsidiary when there is no risk to the bank, or in blocking a company from pursuing new and potentially beneficial opportunities. The potential harm to the company, its bank subsidiary, and its shareholders could be substantial and SIA believes such a threat to an otherwise safe and sound bank could be justified only if there were compelling reasons for imposing restrictions and the definitions were very carefully drafted.

The SIA is aware of no evidence or other basis to conclude that any SIA member owned bank would be inherently more at risk if its parent company does not meet an arbitrary definition of a commercial company or lacks consolidated regulation, as evidenced by the industry's safe and secure record of operations over the past twenty years. For that reason, the SIA opposes adoption of any restrictions on industrial banks generally, or any group of industrial banks, that are not linked to the safety and soundness of the bank or serving public needs and convenience.

The activities restrictions in the Bank Holding Company Act are characterized as necessary to maintain an important public policy separating banking and commerce. In reality, the only valid public policy reason for separating banking and commerce was to ensure equal access to credit when banks were the primary sources of credit. That is no longer the case.

The final argument against the bank centric regulatory system is that the FDIC is not competent to regulate holding companies. Again, the record thoroughly disproves this notion. Many of the strongest banks operating today have developed outside the traditional bank holding company sector of the industry and the experience the FDIC has gained regulating industrial banks and their affiliates has provided it with a level of expertise comparable to any other regulator.

3. *Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based on whether the owner is subject to some form of consolidated Federal supervision? If so, how and why? Should the FDIC assess differently the potential risks associated with ILCs owned by companies that (i) are subject to some form of consolidated Federal supervision, (ii) are financial in nature but not currently subject to some form of consolidated Federal supervision, or (iii) cannot qualify for some form of consolidated Federal supervision? How and why should the consideration of these factors be affected?*

As stated above, all current SIA members with bank subsidiaries are subject to consolidated regulation. Based on that experience, we are aware of no evidence that the lack of consolidated regulation of a bank's parent and affiliates would expose the bank to added risk. For that reason, SIA would strongly oppose any new laws or regulations imposing additional restrictions on banks and their affiliates due solely to the lack of consolidated regulation of a bank's holding company and affiliates.

It is appropriate for the FDIC and state regulators to determine what regulatory oversight of a bank's parent and affiliates is needed to protect the bank and review whether other regulators are performing that task. When regulatory oversight is needed and is not provided by another regulator, or is not adequate, it is appropriate for the FDIC to impose conditions and requirements on that particular bank and its affiliates as a condition of an application or order or as a recommended action in an examination. This is what the FDIC has done in the past and it has worked well to ensure the safety of the bank. Imposing requirements across the board without regard to the risks relating to any particular bank would be arbitrary and capricious and harmful to the financial services markets.

Consolidated regulation is now required by many nations for banks and other financial services companies operating internationally to ensure that at least one qualified regulator has an overview all of the institution's activities. Thus far the FDIC has not sought designation as a consolidated regulator for that purpose. That is not an issue for banks operating only in the U.S. When banks that are not subject to consolidated regulation plan to operate internationally, the FDIC can impose added requirements to oversee those operations if needed, as it has done in the past. The lack of a consolidated regulator is not otherwise a barrier for companies that want to own banks in multiple nations.

4. *What features or aspects of a parent of an ILC (not already discussed in Questions 2 and 3) should affect the FDIC's evaluation of applications for deposit insurance or other notices or applications? What would be the basis for the FDIC to consider those features or aspects?*

The SIA believes the FDIC should evaluate every material and substantial factor relevant to the safety and soundness of a bank and take such actions as may be needed or appropriate to control risks to the bank, the Deposit Insurance Fund, the banking system or the needs and convenience of the public.

As stated above, the SIA does not believe that ownership of a bank by a financial or commercial parent, or the lack of consolidated regulation of a holding company and affiliates, poses an inherent risk to a bank. In contrast, control of a bank by a company or individuals who are incompetent or dishonest poses an obvious risk to a bank and should be dealt with by denying an application or forcing divestiture of the bank. Similarly, control of a bank by a traditional bank holding company could appropriately result in a higher minimum capital requirement and other measures to increase the financial strength of the bank in recognition of the holding company's inherent inability to provide substantial financial support to the bank if needed.

The SIA supports the added requirements imposed in industrial banks to ensure their independent control by competent management. Those are reasonable and logical measures to control affiliate transactions risks when a bank has extensive affiliate relationships within a corporate group. These measures are not unduly burdensome when an industrial bank does not have extensive affiliate relationships.

Similarly, the SIA believes it is appropriate to impose reasonable restrictions on a case-by-case basis to ensure that a bank does not create a monopoly or threaten to diminish needed financial services in a particular area. If a company has a reputation for eliminating competition and leaving areas without supporting businesses, it would be appropriate for the FDIC to impose restrictions to ensure that would not occur if the company were approved to own a retail bank. This would be in accord with the FDIC's responsibility to ensure that a bank serves public needs and convenience.

5. *The FDIC must consider certain statutory factors when evaluating an application for deposit insurance (see 12 U.S.C. 1816), and certain largely similar statutory factors when evaluating a change in control notice (see 12 U.S.C. 1817(j)(7)). Are these the only factors [the] FDIC may consider in making such evaluations? Should the consideration of these factors be affected based on the nature of the ILC's proposed owner? Where an ILC is to be owned by a company that is not subject to some form of consolidated Federal supervision, how would the consideration of these factors be affected?*

The factors in the statutes are broadly worded and will cover the conditions and restrictions described in our prior answers. Beyond the specifically enumerated factors are those things that are implied or must be considered to properly assess the enumerated factors. For example, the adequacy of a bank's information technology systems is not specifically listed among the seven factors in 12 U.S.C. 1816 but is pertinent to an institution's safety and soundness. Other factors are linked to other laws administered by the FDIC. Compliance with BSA and the USA PATRIOT Act are good examples. So, the first test of any factor to be considered when evaluating an application is whether it is based or necessary to enforce a law administered by the FDIC.

The FDIC must also consider whether a regulation or condition imposed in an order or examination conflicts with a statute. In that regard, imposing any restriction or condition on an industrial bank solely because its parent is a commercial company or lacks consolidated regulation (or on the basis of any other factor unrelated to one of the statutory factors) would effectively repeal the exemption of certain industrial bank owners from the Bank Holding Company Act. Congress could have imposed restrictions on industrial bank owners generally or certain groups of owners when it enacted the exemption, but did not. Congress could have authorized the FDIC to adopt limitations to the exemption, but did not. Congress' intent is reasonably clear to allow any legitimate business to own an industrial bank. The FDIC has no authority to act against Congress's will in this regard.

Agencies may not act against the will of Congress *even if there is a rational basis for that action*. See, for example, *Board of Governors of the Federal Reserve System v. Dimension Financial Corporation*, 474 US 361, 88L Ed 2d 691, 106 S Ct 681 (1986) and *First Bancorporation v. Board of Governors of the Federal Reserve System*, 728 P.2d 434 (10th Cir. 1984). The *First Bancorporation* decision invalidated provisions of an order approving an application that classified a NOW account as a demand deposit, and the *Dimension Financial* decision invalidated provisions in Regulation Y classifying a NOW account as a demand deposit. In each case, the court held that the Board of Governors of the Federal Reserve acted contrary to Congress' intent when classifying a NOW account as a demand deposit and the reason for doing so was immaterial.

Even if the reason were material, there is no rational basis for imposing restrictions on industrial bank holding companies based on whether they are commercial or lack a consolidated regulator. The FDIC has expressly said so for nearly twenty years and would potentially be the strongest witness against itself if it suddenly changed its position without any change in the underlying record and that action was challenged in court. Courts can invalidate administrative actions if they are arbitrary and capricious. The Administrative Procedure Act ("APA"), 5 U.S.C. §§ 701 to 706 mandates that reviewing courts set aside agency findings that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. § 706(2)(A). If an administrative action is challenged, agencies are granted deference to their decisions if there is a rational basis for the action taken but a court will "review the evidence anew and determine [for itself]] whether the administrative action was arbitrary and capricious." *First Nat'l Bank of Fayetteville v. Smith*, 508 F.2d 1371, 1374 (8th Cir.1974), *cert. denied*, 421 U.S. 930, 95 S.Ct. 1655, 44 L.Ed.2d 86 (1975); *see, e.g.*, *Hymel v. FDIC*, 925 F.2d 881, 883 (5th Cir.1991). Here, there is simply no evidence in the record supporting a conclusion that a bank owned by a commercial company or an entity not subject to consolidated regulation is a risk to the bank and the Deposit Insurance Fund. For that reason, we believe any restrictions imposed on industrial banks based on those factors would be arbitrary and capricious and therefore invalid.

The strongest objection to a change of policy on holding company regulation would be the impact on the banking industry generally. An agency is required to have a rational basis for its actions in part to assure continuity and certainty in the process. A business must have some degree of assurance of stability when committing resources to a business plan. Sudden and unwarranted changes in the standards applicable to industrial bank holding companies would extensively damage many currently operating banks and the industry generally. It would provide a strong reason for other businesses, potentially including many SIA members, to rule out organizing a bank subsidiary even if that would substantially improve the operating efficiency of that business. Such surprise and unwarranted actions are antithetical to the needs of the market and must be avoided except in extraordinary circumstances outweighing the harm that would be done to the market.

6. *Should the FDIC routinely place certain restrictions or requirements on all or certain categories of ILCs that would not necessarily be imposed on other institutions (for example on the institution's growth, ability to establish branches and other offices, ability to implement changes in the business plan, or capital maintenance obligations)? If so*

which restrictions or requirements should be imposed and why? Should the FDIC routinely place different restrictions or requirements on ILCs based on whether they are owned by commercial companies or companies not subject to some form of consolidated Federal supervision? If such conditions are believed appropriate, should the FDIC seek to establish the underlying requirements and restrictions through a regulation rather than relying upon conditions imposed in the order approving deposit insurance?

See answer to question 5 above. Requirements such as those described in the question if applied "routinely" and across the board or according to classes of bank owners would be unwarranted, unauthorized and unlawful. Conditions such as those described in the question should be imposed only on a case-by-case basis if the restriction or condition is reasonably deemed necessary to ensure the safety and soundness of the institution, public needs and convenience, or compliance with applicable laws and regulations.

7. *Can there be conditions or regulations imposed on deposit insurance applications or changes of control of ILCs that are adequate to protect an ILC from any risks to safety and soundness or to the Deposit Insurance Fund that exist if an ILC is owned by a financial company or a commercial company? In the interest of safety and soundness, should the FDIC consider limiting ownership of ILCs to financial companies?*

See answers to questions above. The question presumes that industrial banks or those owned by commercial companies pose a unique risk to the Deposit Insurance Fund. There is no evidence or good reason to support that presumption. The FDIC should consider limiting ownership of ILCs only if it can establish a rational basis for the limitation and the record thus far would provide more of a basis for prohibiting banks from being owned by traditional holding companies. In contrast to traditional banks, industrial banks in general have proven to be safer, financially stronger and less likely to fail. Perhaps the safest banks of all are industrial banks owned by commercial companies that engage entirely in covered transactions because they have no risk of loan loss. Imposing restrictions on the safest banks that do not apply to riskier banks would literally turn the regulatory system on its head.

8. *Is there a greater likelihood that conflicts of interest or tying between an ILC, its parent, and affiliates will occur if the ILC parent is a commercial company or a company not subject to some form of consolidated Federal supervision? If so, please describe those conflicts of interest or tying and indicate whether or to what extent such conflicts of interest are controllable under current laws and regulations. What regulatory or supervisory steps can reduce or eliminate such risks? Does the FDIC have authority to address such risks in acting on applications and notices? What additional regulatory or supervisory authority would help reduce or eliminate such risks?*

All banks with affiliates engage in various kinds of cross marketing. Indeed, that has become a core marketing plan for most large commercial banks. The anti-tying laws prohibit certain kinds of cross marketing for all banks. A bank with an insurance affiliate has as much of an opportunity to offer discounted loan rates to customers who purchase insurance from its affiliate as a bank owned by a retailer would have to offer incentives to shop at the affiliate. In both cases, the anti-tying laws prohibit the bank from offering the incentive.

Clearly, the FDIC can act on business plans in applications that present or could involve tying issues. The FDIC reviews all applications for compliance with law and a plan proposing to engage in illegal or improper tying can be denied for that reason. In addition, the FDIC has essentially the same authority as the Federal Reserve to examine and supervise the activities of a bank affiliate engaged in improper tying with the bank whether or not there is a consolidated supervisor.

9. *Do ILCs owned by commercial entities have a competitive advantage over other insured depository institutions? If so, what factors account for that advantage? To what extent can or should the FDIC consider this competitive environment in acting on applications and notices? Can those elements be addressed through supervisory processes or regulatory authority? If so, how?*

This question is largely inapplicable to SIA members.

10. *Are there potential public benefits when a bank is affiliated with a commercial concern? Could those benefits include, for example, providing greater access to banking services for consumers? To what extend can or should the FDIC consider these benefits if they exist?*

Many customers of securities companies prefer to do business with a company that offers a broad array of services. There are many reasons for that preference. First, the customer doesn't have to maintain multiple relationships to take care of its financial needs. Second, the customer doesn't have to coordinate the services it receives as much. It can work with one provider to identify all services needed, tailor those services to the customer's needs and avoid overlaps, and obtain volume pricing. Third, a broader relationship can enable the financial services provider to develop a deeper understanding of the customer's business and that can lead to better services. Similar positive advantages can arise in the context of a bank owned by a commercial company as well.

Apart from the foregoing comment, this question is largely inapplicable to SIA member owned banks and is more appropriately answered by companies with direct experience in that subject.

11. *In addition to the information requested by the above questions, are there other issues or facts that the FDIC should consider that might assist the FDIC in determining whether statutory, regulatory, or policy changes should be made in the FDIC's oversight of ILCs?*

The FDIC should look at the record and condition of the entire industrial bank industry. It presents a picture that does not warrant criticism or concern or consideration of the kinds of restrictions and prohibitions referenced in some of the foregoing questions. This is clearly an industry that has done things right. The banks in this industry are generally stronger, safer, better capitalized, better managed, more profitable and better supported by their parent companies than traditional banks. They enjoy strong market support. They are beneficial to the communities where they are based and which they serve. All of the proposals for restrictions and prohibitions referenced above and by industry critics are solutions looking for a problem. No significant problem or systemic threat prompted consideration of these measures. This amounts to an attack on one of the most successful and innovative segments of the banking industry and will, if it leads to restrictions on the industry, potentially strangle one of the best new developments in the banking industry in the past thirty years.

The SIA believes the FDIC must carefully consider the needs and structure of the financial services markets. Like all regulators, the FDIC serves the market. Its role is to stabilize the market by helping to ensure that the banks serving the market operate safely, fairly and honestly. The effectiveness of the regulatory system is adversely affected if the requirements imposed by the FDIC conflict with the needs and structure of the market.

The primary advantage of the bank centric model is that it is the most compatible with the market. Banks are businesses whose success is entirely determined by access to good profitable loans. Banks and their owners must have the ability to structure their operations in the best way to get that business. Nothing is more dangerous to the future of banking and individual banks than imposing arbitrary and unjustified restrictions that limit a bank's ability to serve its customers and go with the flow of the markets.

The provisions in the Bank Holding Company Act limiting activities of affiliates and requiring consolidated regulation of all affiliates conflict with the needs of the market. Financial services have spread throughout the entire economy and have become increasingly important to a wide array of companies. Enabling those companies to operate as efficiently and cost effectively as possible should be an important goal of the regulatory system.

The growth of industrial banks is primarily a result of market forces produced by the growing number of companies that are already engaged in financial services or that plan to initiate such services in the future. Many of these companies, including most SIA members, are among the most advanced, sophisticated and competent providers of financial services anywhere. Many of these companies invented the kinds of services they offer and know the product and their customers better than anyone. These are legitimate, honest businesses that form the backbone of the American economy, not a fringe group. Imposing restrictions on these companies *simply because they are not traditional bank holding companies* is wholly unjustified and would adversely affect the entire economy.

The FDIC has understood these basic principles for many years and has been among the leading regulatory agencies in adapting to the modern financial services markets. That is commendable and should be continued.

12. *Given that Congress has expressly excepted owners of ILCs from consolidated bank holding company regulation under the Bank Holding Company Act, what are the limits on the FDIC's authority to impose such regulation absent further Congressional action?*

See answer to question 5 above.

In closing, the SIA appreciates the opportunity to submit these comments and we hope they are helpful. We look forward to working with the FDIC in the future to continue the safe and sound development of some of the world's leading financial institutions.

Sincerely,

Steve Judge
Senior Vice President, Government Affairs
Securities Industry Association