Talking points for Principals meeting

- One of the issues that the NEC and the DPC have been working on over the last several months at the Deputies level is privacy.

- We think this is an important issue because Americans increasingly feel that they have lost all control over how personal information about them is circulated and used by companies.

- The Vice President has given a commencement address on privacy earlier this year - the President would like to have an event on this on July 31st.

- New technologies have made it easier to create, manipulate, store, transmit, and link digital personally identifiable information. People may disclose personal information about themselves as they travel, fill a prescription at the drug store, visit a Web site, call a 1-800 number, send an e-mail, use a credit card, or purchase groceries using a discount card. Information about these individual transactions may be bought and sold - and companies are now assembling giant "data warehouses" that contain electronic dossiers on the needs, lifestyles, and spending habits of millions of Americans.

- However, privacy concerns often have to be balanced with competing values - such law enforcement, cracking down on "deadbeat dads," free expression, and an investigatory press.

- We have been working on a package of privacy policies that we believe has broad support.

  - It includes both "cross-cutting" issues that affect a range of privacy concerns and targeting sectors or users that are particularly sensitive.

  - It addresses both "offline" and "online" privacy;

  - It encourages self-regulation where possible and identify the need for legislation where necessary; and

  - We think it maintains a balanced approach that recognizes the values associated with the free flow of information and with giving individuals greater control over their personally identifiable information

1. **Privacy coordination**: Designate OMB to increase coordination on privacy issues.

2. **On-line Collection of Information Generally**: Continue to press for industry self-regulation - with the option for a legislative solution if self-regulation proves to be inadequate.//

3. **On-Line Collection of Information from Children**: Call for legislation that would specify a set of fair information principles applicable to the collection of data from children (e.g. no collection of data from children under 13 without prior parental consent).

4. **Government Information -- privacy dialogue with state and local governments**: Initiate a "privacy dialogue" with state and local governments about the privacy of personal information collected by governments.

5. **Medical records**: Call for legislation on privacy of medical records consistent with HHS report. [Note: we need some steps the President can take through Administrative action.]

6. **Financial records**:

- Call for regulators to issue regs to make FCRA "opt-out" options more evident to consumers. for sale

- Call for amendments to Fair Credit Reporting Act to limit the "affiliate sharing exception." Businesses could share consumer information for marketing purposes, but not for business decisions. For example, consumer information provided to an insurance affiliate could not be used to deny a person a loan without FCRA protection. [Treasury opposed]

Examine practices

- Give regulators ability to write rules to enforce FCRA. [Treasury and Commerce disagree whether this job should go exclusively to the Fed or joint Fed/FTC.]

- Study of effectiveness of FCRA.

- Review whether reg. Review process for mergers should include a consumer protection analysis [Treasury opposed.]

7. **Profiling**: Encourage other companies that engage in profiling to adopt self-regulatory principles similar to Individual Reference Services Group. [Note: Commerce dropposed the legislative proposal here -- we may wish to put it back on the table.]

8. **Identity theft/theft of personal information**: Fradulent use of another person's identity to facilitate the commission of a crime.

- Endorse the Kyl bill.

- Make it illegal to record social security numbers on checks. [This may be too small.]

- Target those situations in which an offender obtains information illegally but then uses it for a legal purpose (pretents to be a bank customer but sells the information to a private investogator).

9. **Protection of new types of information**: Study on new types of personal information -- such as biometrics.

10. **Public education**: Work with the private sector and non-profits to develop an advertising campaign to inform individuals about how to exercise choice with respect to the collection and dissemination of their personally identifiable information.

THE WHITE HOUSE

WASHINGTON

August 7, 1998

The Honorable Alfonse D' Amato
Chairman, Committee on Banking
U.S. Senate
Washington, D.C.

Dear Mr. Chairman:

This Administration has been a strong proponent of financial legislation that would reduce costs and increase access to financial services for consumers, businesses, and communities. Nevertheless, we cannot support the Financial Modernization Act of 1998, H.R. 10, which is now pending before your Committee. In the form that the bill is currently drafted, it would stifle innovation and efficiency in the national banking system, and impose needless costs on small banks. In addition, the Administration believes that the bill would materially weaken the national banking system by depriving national banks of the powers they now have and would erode the ability of the Executive Branch in formulating and implementing financial institution policy.

I share your perspective that an overhaul of the laws that regulate our nation's financial services industry is long overdue. However, the President will veto the bill if it is passed in this form.

With best wishes, I am

Sincerely,

Erskine B. Bowles
Chief of Staff

(http://aspe.os.dhhs.gov/admnsimp/index.htm)

FINANCIAL INSTITUTIONS AND PRIVACY
Talking Points: August 17, 1998 -- DRAFT

CLOSE HOLD -- NOT FOR DISTRIBUTION -- FOR DISCUSSION ONLY

- The Administration strongly opposes H.R. 10. The Chief of Staff has indicated that the President will veto the bill if presented to the President with its current significant deficiencies.

- As a result, the Administration opposes a strategy to offer desirable amendments to address concerns about consumer privacy, which may only serve to make it more attractive for wavering members -- especially Democrats -- to support H.R. 10.

- If such amendments were offered, while we might (or might not) support their substance, they would not change our position on the underlying measure.

- However, in response to your request, we will detail for you the Administration's current position on privacy of consumer financial and other information. We would welcome an opportunity to work with you to advance appropriate legislation in another context.

- **Voluntary and Self-Regulatory Privacy Guidelines.** As a general matter, the Administration supports and encourages the efforts of industry and self-regulatory bodies to develop privacy standards appropriate to their specific industry, based on certain principles. These principles include _____. However, in certain cases, where adequate voluntary steps are not taken or where the privacy interests at stake are too important to await appropriate voluntary response, the Administration supports legislation.

- **Vice President Gore's Privacy Announcement.** The Vice President recently announced ~~a number of~~ proposals to protect consumer privacy, including:

  - **Identify Theft:** The Administration supports Senators Kyl and Leahy's bill to crack down on the fraudulent use of another person's identify to facilitate the commission of a crime, such as credit card fraud. (This bill has passed the Senate and awaits House action.) (S. 512)

  - **Theft of Personal Financial Information:** The Administration supports legislation sponsored by Representatives Leach and LaFalce that will make it a federal crime to obtain confidential customer information from a bank by fraudulent means. (In some cases, people are obtaining information illegally and then using the information for a legal purpose -- e.g., pretending to be a customer in order to trick confidential information out of a bank, and then selling that information to a private investigator or other third party.) (HR 4321)

202-690-5882

- **FCRA Information Sharing Disclosures and Opt-Outs.** The ~~Fair Credit~~ Reporting Act (FCRA) permits sharing of personal information with affiliates; however, the consumer must be provided with notice that their information may be shared and given an opportunity to opt-out of the affiliate sharing. (Note that this notice and opt-out right does not apply to "transactional" and "experience" information which may be shared with affiliates or sold to third parties without notice or right to opt-out.) The Administration has directed the Treasury and the bank regulators to work together to strengthen enforcement to ensure compliance with these requirements. ***[BAER TO CHECK ON FED INTENTIONS.]*** Steps may include development of "best practices" for financial institutions and enforcement actions against these and other types of firms.

- **FCRA Examination Authority.** The FCRA permits sharing of personal information with affiliates; however, the consumer must be provided with notice that their information may be shared and given an opportunity to opt-out of the affiliate sharing. (Note that this notice and opt-out right does not apply to "transactional" and "experience" information which may be shared with affiliates or sold to third parties without notice or right to opt-out.) The bank regulators, however, are prohibited from examining financial institutions for compliance with these notice and opt-out requirements. The Administration supports legislation to allow regulators to monitor financial institutions for compliance with the law.

- **Medical Record Privacy.** On September 11, 1997, HHS Secretary Shalala recommend Federal legislation to protect the confidentiality of health information by imposing duties on those holding such information and providing rights to the subjects of the information. She proposed that Federal law provide a floor of protection and that the States be permitted to provide stronger protections, in addition.

e.g. - self-insurer employer - process claims but can't use the info in making personnel

  - Under the legislation, health care providers, those who pay for health care, and those who get information from those entities would have to:
    - permit patients to see their own records
    - keep records of disclosures and let patients know who has seen their records,
    - permit patients to file proposals for correction of erroneous records
    - advise patients of their confidentiality practices and the patient's rights.

  - Under the legislation, disclosure would only be permitted if authorized by the patient or for specifically authorized purposes including:
    - treatment and payment
    - research
    - public health

- oversight of the health care system
- use in law enforcement or other legal proceedings permitted by law.

- Within an organization, information could be used only for the purposes reasonably related to the purposes for which it was gathered and disclosures would have to be limited to the minimum necessary to accomplish the purpose of the disclosure.

- Entities receiving information pursuant to patient authorization would have to give patients a statement of their intended use of the information, and would be civilly liable for uses in violation of that statement.

- In addition, there would be civil and criminal sanctions for violations, such as improper disclosure and obtaining information under false pretenses.

State, Health

- ***Spell out in detail how the provisions we support would apply in context of insurance firm merger with financial company.***

- Administrative steps:

- **Other Proposals.** In addition to these steps, already announced, further steps along these same lines could be taken to enhance consumer privacy.

Possible legislation

- **Legislative Specification of Notice and Opt-Out Requirements for Affiliate Sharing.** No agency has rulemaking authority under the affiliate sharing provisions of the FCRA (which allow sharing of personal information with affiliates), although the Federal Reserve has the ability to issue interpretations and the bank regulators and the Federal Trade Commission (FTC) can enforce its provisions. However, the requirements in statute are sketchy -- there is no commonly understood: (1) definition of what information is personal and is subject to these requirements; (2) what information can be shared and with whom; (3) what constitutes "clear and conspicuous" notice; and (4) what constitutes providing the consumer with a reasonable opportunity to opt-out. While the bank regulators have some ability to strengthen enforcement, ***it would be easier to enforce if the statute more specifically prescribed the standards for consumer notice of their rights and mechanisms for exercising those rights.***

- **Limiting the Undisclosed Sharing and Selling of Consumer Transactional Information.**

  - The Fair Credit Reporting Act (FCRA) as enacted in 1970 exempted from the definition of "consumer report" the communication of "transaction or experience" information.

- The purpose of the exemption was to facilitate communication of information by credit grantors and others to credit bureaus, by not making the furnishers of that information subject to the restrictions of the FCRA.

- This system has resulted in huge benefits to the economy by allowing firms to quickly and efficiently assess the risk posed by consumer applicants for credit, insurance, or employment, for example. Consumers have benefited too, for example, by being able to buy a car in an hour's time or obtain credit as they enter a department store for the first time.

- However, the exemption for reporting of experience or transaction information also allows credit card issuers, banks, and insurance companies, for example, to sell detailed transaction information about their customers without disclosure, opt-out rights, or other restriction.

  - Some consumers may view it as a benefit that firms can target catalog mailings, for example, to their interests (e.g., biking, travel, gardening, pets).

  - However, others may view the sale of their transaction information as an invasion of privacy, especially when it results in third parties learning about their medical or financial condition.

  - The rapidly expanding use of computers to cull through and compile information means that this type of information sharing occurs much more frequently than in 1970 when the FCRA enacted.

- In 1996, Congress amended the FCRA to allow affiliated companies to pool certain personal information without being treated like a credit bureau, as they would have been prior to the amendments.

  - However, before information can be shared with an affiliate, consumers must be: (1) told that their information may be shared with affiliates; and (2) given an opportunity to opt-out -- to insist that their information not be shared.

  - These procedures do not apply to transaction or experience information when shared with an affiliate. That information benefits from the broader exemption in the FCRA regardless of whether the information is shared with an affiliate or other third party.

- The FTC is planning a one-year study of what protections should be afforded exchange of transaction and experience information, including an assessment or the costs and benefits of additional protections.

    - The study is motivated, in part, by concern that, in a computer networked world, the credit bureau as we know it will become obsolete. Instead, it will become far more efficient to poll one or more firms directly over a network about a specific consumer applicant. Under the experience or transaction exemption, the resulting exchange of information would fall outside of the FCRA's protections.

    - Similarly, as firms increasingly merge with targets to gain access to information about the target's customer base, new questions are raised about the affiliate sharing exemption.

- The FTC will consult with the banking agencies in designing and implementing its study, as well as in developing recommendations.

- ***A Congressional mandate for such a study might prompt greater voluntary steps in the interim and ensure that its recommendations receive prompt attention by the Congress.***

DEPARTMENT OF THE TREASURY
Office of Financial Institutions
1500 Pennsylvania Avenue, NW
Washington, DC 20220

TO: **SARAH ROSEN**
Senior Advisor, National Economic Council
Addressee's fax number: 456-~~2233~~
5802

FROM: **RICHARD S. CARNELL**
Assistant Secretary of the Treasury

Telephone:	**202/622-2600**
Fax:	**202/622-2027**
Internet:	**RICHARD.CARNELL @TREAS.SPRINT.COM**

DATE: **September 22, 1998**

Number of pages to follow: 20

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

CLOSE HOLD

MEMORANDUM FOR ERSKINE BOWLES
GENE SPERLING

FROM: Robert E. Rubin

SUBJECT: Meeting on Financial Modernization with Citicorp and Travelers Group

We are scheduled to meet tomorrow with Sandy Weill of Travelers Group and John Reed of Citicorp. Both can be expected to argue strongly for enactment of H.R. 10, the financial modernization bill. The Administration has strongly opposed the bill passed by the House and approved by the Senate Banking Committee. That bill would (in both forms) greatly diminish the role of the elected Administration in financial services policymaking and adversely affect the Community Reinvestment Act (CRA).

Prospects for the Bill

H.R. 10's proponents are hoping to bring the bill to the Senate floor late this week or early next week.

Factors Working in Favor of the Bill

- Large banks, securities firms, and insurance companies recognize the benefits of affiliating with one another (such as cross-selling opportunities and efficiency gains), and tend to strongly support the bill.

- The House Republican leadership takes considerable pride in moving legislation on a subject that long stymied Democratic-controlled Congresses. Likewise, Senator D'Amato -- under attack for the paucity of his legislative record -- wants to demonstrate his skill in moving difficult and complex legislation.

- Senator Lott has committed himself to move the bill, and Senator Daschle favors the bill.

- Senator Sarbanes (who favors the bill because it separates banking and commerce) is privately telling Democratic Senators that if H.R. 10 does not become law this year, Democrats will end up with worse legislation in the next Congress, which he expects to be significantly more Republican.

Factors Working Against the Bill

- Congress is scheduled to remain in session for only three more weeks.

- The Administration has stated that the bill faces a veto.

    - And if final Congressional passage (including resolution of House-Senate differences) occurs after the middle of next week, a pocket veto may also become an option.

- The bill faces resistance from diverse quarters in the Senate, and some 20 Senators reportedly have placed holds on the bill.

    - Populist Democrats -- led by Senator Dorgan, and working with consumer and community groups -- assert that the bill would concentrate economic power, erode safety and soundness, and undercut the CRA.

    - Senators Gramm and Shelby -- never enthusiastic about the bill -- oppose it because it would make CRA compliance a precondition for initially obtaining broader powers and would also extend the CRA to the new, FDIC-uninsured wholesale banks that the bill permits.

    - Miscellaneous interest groups object to, or demand changes in, the bill. For example, many bankers (especially small bankers) criticize the bill for going too far in subjecting banks' insurance-sales activity to discriminatory state laws, whereas insurance agents attack the bill for excessively curtailing state laws. Some companies that own thrift institutions object to restrictions on the companies' activities that would apply if the companies were ever sold.

Our Strategy

The debate over conducting new financial activities through "operating subsidiaries" of banks basically comes down to three activities: securities underwriting, merchant banking, and insurance underwriting. The Treasury proposal included all three, the House Banking Committee bill included securities underwriting, and the current bill includes none. We have already publicly proposed ways of assuring that the Federal Reserve Board retains a jurisdictional reach over large national banks. But the Fed has thus far ruled out compromise on the issue of subsidiaries.

We have been developing a possible compromise which could be discussed with Congressional leaders at the appropriate time.

We have been wary of entering into negotiations prematurely -- lest word of such negotiations dismay the bill's remaining opponents, give impetus to legislation, and thus undercut our leverage. We are also seeking reasonable assurance that such managers of the bill as Senator D'Amato would negotiate seriously, and -- if they reached agreement with us -- would not renege in the face of objections from the Fed.

TALKING POINTS
for meeting with Sandy Weill and John Reed
September 23, 1998

[Note: Weill and Reed are among H.R. 10's most ardent supporters. They will eagerly report to their Congressional allies any implication that the Treasury's opposition to the bill lacks White House support. By the same token, a reaffirmation of White House support for the Treasury's position may finally bring the bill's proponents to the bargaining table.]

- H.R. 10 is gravely flawed.
    - The bill would, in numerous ways, undercut the role of this or any future Administration in financial services policymaking.
        - It would allow new financial activities to be conducted only in entities regulated by the Fed (e.g., securities affiliates, insurance affiliates, wholesale financial institutions, and overseas subsidiaries) -- thereby devaluing the national bank charter. It would make the Fed the sole banking regulator for bank holding companies, for all new financial activities authorized by the bill (e.g., securities activities, merchant banking, and insurance underwriting), and for the new wholesale banks created by the bill. National banks would then have a strong incentive to switch to a state charter, pick up the same regulator as their affiliates, and shed a superfluous regulator (Treasury/OCC).
        - *In so doing, it would upset the existing balance between the elected Administration and the independent agencies -- diminishing the role of the elected Administration in a critical area of economic policy-making.*
    - There is no good reason for doing this. It does not help safety and soundness, and is not necessary for functional regulation.
        - Allowing activities in subsidiaries would promote safety and soundness (as the FDIC points out).
        - Citibank already has a $70 billion subsidiary underwriting securities and conducting merchant banking abroad. This activity, permitted by current law and subject only to Fed regulation, belies any argument that these activities are unsafe for subsidiaries of banks. Other financial institutions should have the same sorts of choices about how they structure themselves.

- The bill would also do little for communities and consumers, and would actually tend to weaken the Community Reinvestment Act. It would:

    - encourage the movement of assets, activities, and innovation out of banks (where they can contribute to the banks' CRA activities) and into holding company affiliates; and

    - permit wholesale institutions (such as J.P. Morgan and Bankers Trust) to have full access to the discount window and the payment system while avoiding the CRA.

- We see no reason to accept such a badly flawed bill -- a bill that so dramatically (and gratuitously) reorders financial regulation against the Administration and in favor of the Fed.

- We have made proposals to bridge the gaps here, but have received no response.
  (For example, at the June 1 Senate hearing, Secretary Rubin suggested requiring the largest banks to retain holding companies so as to assure that the Fed has jurisdiction over them.)

BACKGROUND INFORMATION FOR GENE SPERLING: CHANGES MADE BY SENATE BANKING COMMITTEE

The Senate Banking Committee made the following major changes in the House-passed bill:

- Adopting a complex set of adjustments to the provisions governing the insurance sales activities of banks and affiliated companies. These changes generally tend to narrow the leeway provided by the House bill for State insurance regulation to discriminate against banks and their affiliates. The bill would still curtail judicial deference to the Comptroller of the Currency's insurance-related interpretations of the National Bank Act, providing deference only regarding certain state laws adopted before September 1998.

  Insurance agents complain that the bill goes too far in the banks' direction, while the OCC and many banks (especially small banks) contend that the bill provides too little protection against discrimination.

- Narrowing the House bill's requirement that banks transfer certain kinds of financial activities to broker-dealers registered with the Securities and Exchange Commission. For example, the bill would now authorize the Fed (rather than the SEC) to determine that a given activity involving a banking product should be allowed to remain in the bank.

  Representative Dingell complains that the Senate bill overly narrows the House bill's transfer requirements.

- Deleting the House bill's requirement that banking organizations that seek broader powers must offer low-cost bank accounts.

- Giving the Treasury some limited voice in the process of determining whether particular activities are financial.

- Extending the CRA to so-called wholesale financial institutions (i.e., banks with no FDIC insurance but with full access to the Fed discount window) only if they have FDIC-insured affiliates.

  Senators Gramm and Shelby contend that even this application of the CRA to wholesale financial institutions goes too far.

- Not authorizing regulators to require divestiture of new financial activities if an affiliated bank has a bad CRA record.

- Limiting the enforcement authority of the OCC and FDIC over subsidiaries of banks.

  The OCC and OTS are looking into whether this raises safety and soundness concerns.

- Generally not permitting transfer of a grandfathered S&L holding company.

  Some S&L holding companies, led by Washington Mutual, vigorously oppose this provision.

- Deleting House provisions that would have cleared the way for mutual insurance companies to shift their domicile to another state and convert from mutual to stock companies.

  Consumer groups opposed these "redomestication" provisions as overly fraught with potential for abuse of companies' existing policyholder-owners. The New York banking and insurance commissioner, Neil Levin (a D'Amato ally), feared significant loss of his insurance regulatory clientele, since New York does not permit demutualization. Life insurance companies strongly urge restoring the provisions to the bill.

To: Secretary Rubin
From: Lisa S. Andrews
Subject: Industry Positions on H.R. 10
Date: September 22, 1998

MEMORANDUM

Despite several near death encounters, HR 10 manages to survive thanks in large part due to the extraordinary efforts of its core advocates: Merrill Lynch, Citicorp/Travelers, and Nation's Bank/Bank of America. The securities industry has remained a strong supporter throughout Congress' consideration of this bill. SIA, the Securities Industry Association claims that they could support op subs, but the House Commerce Committee would not accept this provision. It is not an important enough issue for them to weaken their support.

As a result of changes the Senate Banking Committee made, the American Bankers Association now supports HR 10. The ABA has persuaded most state banking associations to support the bill, with the exceptions of OK, TX, KS and KY. ND opposes, too, but may become neutral. Those opposing view the 13 safe harbors in the bill as creating too much opportunity for states to enact laws discriminating against banks offering insurance. Apparently, the memo from the OCC addressing this issue has generated much concern among the state associations. The Independent Bankers Association has taken a position of "not opposed," but earlier enunciated support for the affiliate structure. (Ken Guenther of IBAA worked for the Fed.) America's Community Bankers Association wants to make improvements in the bill, particularly the thrift provisions and allow for full transferability of grandfathered powers. ACB would like all of Title IV removed, notably Sec. 401.

A number of large banks have also changed their position to one of support. Walter Shipley of Chase Manhattan just sent a letter expressing support to the Senate provided the bill does not change. Last week, Norwest, one of the last holdouts opposing the bill, agreed to join the Bankers' Roundtable support of the bill. Both Norwest and the Roundtable have been advocating the need for addressing op sub. Washington Mutual, the Nation's largest thrift, however, has persuaded Senators. Gordon and Murray to place a hold on the bill because of its restrictions on the transfer of grandfathered unitary thrifts.

The insurance industry had been a strong supporter of the House passed bill, but the agents now strenuously oppose the Senate passed version. The agent groups, the National Association of Underwriters ("NALU") in particular, have tried unsuccessfully to reach an agreement with the American Bankers Association to settle their difference on the insurance sales provisions. Consequently, the Independent Insurance Agent and the Professional Insurance Agents have mounted major grassroots campaigns against H.R. 10. NALU has or is expected to activate their membership as well. These associations purportedly have lined up Senators Ford, Bob Kerry and Cleland to fight their battle on the Senate floor. Should the bill pass the Senate, the agents have much support in the House, particularly with Speaker Gingrich and Rules Committee Chairman Solomon who would be key members deciding on whether to accept such a bill.

The insurance company trade associations generally continue to support HR 10, but have a few issues they would like to see addressed concerning corporate governance and state discrimination. The removal of the redomestication provision has created a tremendous internal problem for the ACLI. Their big NY-based mutual member companies, e.g. Metropolitan and New York Life, are adamant that this provision be restored. This creates a political problem for D'Amato, who cannot be seen supporting legislation that would allow major NY mutual companies to redomestic to states where they can demutualize.

Several community groups have launched their own grassroots campaigns to defeat HR 10. They have been especially energized by the weakening of the Community Reinvestment Act. The National Community Reinvestment Coalition are looking to Senators Wellstone, Dorgan and Feinstein for help with their cause.

In summary, the question of whether the banks and the insurance agents can cut a deal remains a central factor in the prognosis for the bill. If an agreement can be reached between these groups, then the changes for enactment dramatically improve. The next question becomes whether the House would accept such a brokered agreement.

Industry Positions on H.R. 10

I. Insurance

Paul Equale of the **Independent Insured Agents** confirmed that they are negotiating with the ABA to come up with a compromise on the insurance provisions. He assured me that they had a "fireball built on the Senate floor to protect their interests if necessary. He mentioned Bob Kerry, Wendall Ford, Max Cleland, and implied other midwestern populists were supporting them. On Friday, Sept. 18, Paul said he had just come from a meeting with Sarbanes and his senior staff to explain their concerns on the insurance provisions. Sarbanes, Dodd and D'Amato really want a bill and Paul seemed quite hopeful that their issue would be addressed. He said that during the S. Banking mark-up, the agents had been asked "to look the other way," which some took to mean they approved of the bill tacitly. Paul said they had corrected that misconception. He commented that Bahner is trying to find a way to move a bill which would be no worse for the agents than the House bill. Subsequently, Tom Conklin of the Indep. Insurance Agents, reported no agreement has been reached with the ABA. He lamented that they do not have a strong Member of the Senate willing to serve as a broker between the entities.

NALU (Nat'l Ass. of Life Underwriters)-- David Winston does not believe an agreement can be worked out; hence, the grassroots effort. He said neither D'Amato or Sarbanes seem willing to accept a manager's amd. He commented that the ACLI has a huge problem -- ie the redomestication issue. David also said that no one seems to be lobbying the rank and file Senators, eg, Lautenberg said no one from private industry had been in to talk about HR 10. He assured me Sen. Ford would be a dog fighting this battle for them; "Ford is more adament than we are." He reiterated that he sees no incentive for the banks to concede. NALU is mounting a big grassroots campaign to defeat the bill.They've called upon their entire membership -- a rare event. They also just ended a national convention where they were reving up opposition. View they bill as worse than current law. They hope the bill dies.

According to the **PIA**, the Professional Insurance agents (p&c agents), the agents have not reached an accord with the ABA, nor do they believe agreement is likely. Consequently, the grassroot effort to defeat the bill continues in earnest. PIA faxed 22,000 members last week, NALU sent some 80-100,000 legislative alerts to their membership. PIA said they're getting a good response, but Marne reports she's heard little on the Hill about the agents' grassroots lobbying.

Lincoln National (members of ACLI and the Financial Services Council) -- Interestingly, Mark Pope shared with me that Howard Mennell has agreed to a manager's amendment, a technical amendment and an agreement to work out redomestication in conference. One part of the manager's amd. would cure a huge problem concerning state corp governance. As Mark explained it to me, HR 10's provision pre-empting state laws that prevent or restrict affliations also captures state "corp. goverernance laws" which help protect companies from unwanted takeovers. He said the ACLI has gotten SIA aboard on this, that it's critical to the IBAA, and that the ABA wants it, too. Mark even said it's on page 10 of the manager's amd. I asked if he had a copy he could share. He said that this is the only part he had, which I find hard to believe. The header on the fax shows page 10 orginated from the Board of Governors two days ago! While the substance of the provision is not critical here, the fact that Howard has a manager's amd. seems indicative of movement. The technical amendment relates to Sarbanes' "mega-merger amendment" by adding a third criteria for the Fed to consider if a target company in a takeover has assets of greater than $40billion. This provision would require the Fed to consider the functional regulator's opinion on whether the merger would protect the interests of policyholders and the risk to the state insurance guaranty fund. He commented that without these amendments, then the IBAA would really come out opposed.

II. Securities Associations

The **SIA** fully supports HR 10 and supports an affiliate holding structure for the ease of functional regulation. Steve Judge said that while they prefer the affiliate approach, they are "agnostic" about the op sub structure. He said they had been willing to talk about flexibility for op subs earlier, but that the House Commerce Committee was adamantly opposed. Steve thinks there's a 50-60% chance the bill will pass the Senate, and commented that neither the Fed or Treasury thinks the bill will really become law. He volunteered that if Rubinand Greenspan, or Summers and Virgil Mattingly (or whoever's #2), could get together then they should be able to work out an agreement. I reminded him that we hadn't been able to do that earlier and remain staunchly opposed to the bile.

III. Individual Banks

First Union's Chairman Crutchfield said at the CEO lunch 9/17 that they supported H.R. 10. His Washington lobbyist, however, told me that First Union was not actively supporting the bill. Joe Siedel said it was a bad bill, and that Wachovia and all the other N.C. banks [except Nation's] were against it. FU's top exec's were in town 9/17 for the BRT meeting. Their sec. sub., Wheat First, exec. was in, too. These exec's lobbied with the message that progress was made in HR 10, but it was not enough. FU has problems with the safe harbors enabling states to enact discriminatory state laws against financial institutions. They have a particular problem with Fla.'s insurance commissioner and this language could exacerbate that problem. FU is studying this provision carefully.

Norwest is now supporting the bill. They apparantly joined in a Merrill Lynch letter today expressing their support. Anita Bedelis said they were pushing op sub hard, arguing among other reasons that the Fed had an imbalance of power. She reported Dorgan, Wellstone, Feingold all agree on the Fed problem. Norwest will continue to support the bill, however, even if op sub is not taken care of. They would also like to see clarification on the ins. provisions. Anita said they are very worried about the potential for the House bill to be enacted (which they oppose). She says Daschle would like to move something because of Sarbanes, but that he listened carefully to Kovacevich on the need to curb the Fed's authority and on the op sub issues. Norwest views the Senate as an interim battle.

Chase's Chairman Shipley sent a letter to the Senate expressing Chase's support for the bill provided no changes are made. Rick Hohlt said the report was filed Friday and that Lott is expected to bring the bill to the floor on Oct. 2, conceiveably it will be a bill the House will accept. Rick says they recognize there's not enough time for a conference.

IV. Bank Associations - National

As Jerry reported earlier, the **Bankers Roundtable** now supports H.R. 10. Alfred Pollard said they are focusing on the op sub issue and the fact that the Fed has too much power under this bill. He also said Daschle was going to encourage Reed to take the lead on op sub. If no ob sub amd were adopted, the BRT would continue to support the bill. In their lobbying materials, the BRT include 2 pro op sub editorials [and a pro IMP piece.]. When Larry spoke to the BRT Sept. 18th on the international economic situation, no one asked a question on the HR 10.

America's Community Bankers-- wants to make improvements in the bill, particularly the thrift provisions and allow for full transferability of grandfathered powers. ACB would like all of Title IV removed, notably Sec. 401.

V. Bank Associations - State

I have spoken to numerous state banking associations this week and with the exception of the ND, TX, OK and KY, all are inclined to support HR 10. The lack of enthusiasm is evident. ND is opposed now, but may become "neutral" at best. Their Exec. Director said Dorgan would oppose no matter what and that Conrad was opposed.

The **Arkansas bankers** view HR 10 as much improved to the point, "It's digestible, with heartburn." They have grave concerns about slippage occur on the bill, especially in -conference. Their concerns over unitary thrifts and deterrence have been ameliorated and are sharing this with their Senators. He noted the lack of improvement on op subs. The Ex. Dir. senses that the Senate is being asked to pass legislation without much opportunity for a thorough debate. Nevertheless, the "emotional issues" for bankers -- unitary thrifts and the ability for state ins. comm'rs to discriminate have been taken care of to a degree they're satisfied.

The **WV bankers** hold a similar view. They are satisfied with the unitary thrift and title ins. provisions, which had been their chief sources of opposition earlier. He expects that at some point they will lobby for the bill. He noted that the ABA is pushing hard on op sub.

KS Bankers -- After a week of regional meetings, the KS bankers are ambivalent about HR 10. They really don't care whether it passes or not, and have expressed this position to their Senators whose staffs have called asking their position. Jim Magg thinks their Senators will follow the state ass'ns recommendation. Presently, their position remains opposed, but it may change after the ABA conference call. Jim said KS doesn't have problems with their insurance commissioner, and 70% of their members are in towns of less than 5,000 so already are eligible for ins. powers. Op sub not a big deal, but a few urban county bankers would prefer op. sub. Jim commented that Roger Beverage of OK Bankers had sent around the OCC memo.

LA does not have a position yet since they have only seen a one-page summary. They had been opposed to the bill, and don't have an official position now. He warned that the House leadership has made no commitment on [preserving] the Senate language and doesn't believe Congress can be trusted to develop a bill acceptable to the industry.

The **MT bankers** are not that concerned about the bill since most of their members are rural bankers who would not interested in expanded powers. They have given up on engaging in the legislative debate since losing the credit union vote. Although the MT bankers usually follow the ABA's position, the Ex. VP/CEO thought they'd be more inclined to follow Norwest's position (supportive or the IBAA's. Bottom line: they're not actively lobbying this.

Iowa has no official position until a Board meeting is held, but probably could support the bill based upon what they've seen. IA is unique in that state banks have security powers option already; for the national banks, they're concerned about state discrimination; feel that the tightening on unitary thrifts is all they can get; agree w/ Treas. on op sub, but believes few community bankers would offer insurance in subs.

ID is ambivalent about the bill. Largest member, US Bank has been for HR 10, but others had been opposed. The ass'n probably won't oppose the bill or lobby aggressively for it. The Exec. Dir. lamented that their Senators weren't that concerned about the bill all along and she expected them to follow the Republican leadership on this bill regardless of the ass'n's position. She had heard that the FHLB in their district had problems with the governance issue. and suggested that the FHLBs might be allies in opposing the bill. She was checking on this. The ass'ns board meets Sept. 23 and will likely have an official position then.

AK Bankers -- They can probably support the bill, and will likely lobby on it later. They only have 8 banks in AK, including Key and B of A. Right now, the Ass'n is concerned with ATM fees in the bankruptcy bill. In terms of HR 10, they're concerned about a prohibition on title ins. sales by banks not already in the business; that lifeline banking is a major negative if restored; believe CRA has gone too far and creates an competitive adv. for those not subject to it. Have no concern with op sub; no problem with Wolfies. He feels no pressure on bank ins. sale. (seems contrary to concern @ title ins.) Believes that there's little real enthusiasm for the bill, but that bankers view think this bill is better than what they'd get next year. Another driving factor for bankers' support is that big interests will use the unitary thrift charter to banks' competitive disadvantage. Bottom line, though, he personally think that there's too much in the bill to get it enacted into law.

OK against, says both Senators oppose based upon their discussions; ins. provisoes too unclear, nothing for community banks. TX opposed due because of problems with safe harbors.

FL --supports bill, and Connie Mack apparently supports because of Barnett i.e., Nations.

Miss. Bankers met 9/21 with the ABA and the ACB jointly. Apparently, the ass'n is torn on its support for HR 10. While one of the members was a strong proponent at the meeting, others had concerns with the 13 safe harbors and expressed fear that they may generate new, unfavorable state laws. ABA purportedly did a poor job explaining these provisions. Accompanying the ass'n were the state's Banking Commissioner, the Deputy Banking Comm'r and the chairs of the state's legislative banking commitees. They're meeting with the Comptroller tomorrow. Steve Verdier called Carolyn McFarlen to warn her about the lack of unity among the MS bankers and the fissure on the state powers. The MS bankers will also meet with Lott who wants to know where they stand. Presumably it will influence how strongly he feels about moving the bill.

Media Advisory

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

September 23, 1998

Attention: Banking Reporters/Business Editors

The attached letter from acting Comptroller of the Currency Julie L. Williams and Office of Thrift Supervision Director Ellen Seidman was sent to Senate Banking Committee Chairman Alfonse M. D'Amato. An identical letter was sent to Sen. Paul Sarbanes, the Banking Committee's ranking Democrat.

In the letter, the two regulators express grave concern with a provision added by the Senate Banking Committee to the financial modernization legislation that limits their agencies' authority to examine and even to obtain information about the operations of securities or insurance units owned by or affiliated with nationally-chartered banks and thrifts.

OFFICE OF THE COMPTROLLER OF THE CURRENCY
OFFICE OF THRIFT SUPERVISION

September 22, 1998

The Honorable Alfonse M. D'Amato
Chairman
Committee on Banking, Housing, and
Urban Affairs
U.S. Senate
Washington, D.C. 20210

Dear Chairman D'Amato:

We are writing to inform you about grave concerns we have with Section 118 of H.R. 10 as added by the managers' amendment that the Committee adopted during consideration of the bill on September 11. This provision compromises our ability to oversee the safe and sound operation of the institutions we supervise. Despite this erosion of the supervisory authority of the Office of the Comptroller of the Currency ("OCC") and the Office of Thrift Supervision ("OTS"), neither of our agencies was informed about this provision prior to its passage nor provided with any opportunity to comment on its effect on the safe and sound operation of national banks and savings associations. This amendment would undermine the safety and soundness of the insured depository institutions regulated by our two agencies. Further, it would weaken consumer protections and appears to be inconsistent with section 307 of H.R. 10, which requires the federal banking agencies to adopt consumer protection regulations in connection with the sale of insurance products by depository institutions and their subsidiaries.

Specifically, Section 118 of the reported bill would limit our agencies' ability to examine, request reports from, and take enforcement actions against functionally regulated insurance and securities subsidiaries and affiliates of bank holding companies (including nonbank subsidiaries of depository institutions). Under the amendment, our agencies must meet rigid standards to justify an on-site examination or to take an enforcement action against a regulated subsidiary. Our examination staff would have to demonstrate that (i) a subsidiary's activities pose a "material risk" of harm to a related depository institution, or (ii) it has "reasonable cause to believe" a subsidiary is not in compliance with laws relating to transactions with a depository institution and it cannot make the compliance determination through an examination of the depository institution. We would essentially be forced to wait until a danger or violation materializes before we could act. Section 118 thus would take away from regulators one of their most important tools to ensure safety and soundness: the ability to act promptly to prevent or contain risks to the depository institutions that they supervise based on their seasoned judgment.

Currently, we work cooperatively with the functional regulators of our subsidiaries and affiliates under flexible arrangements that permit us to examine subsidiaries as necessary. Neither the OCC nor the OTS seek to be the regulator of securities firms, insurance companies, or mutual funds. We fully recognize and respect the primary role of the securities and insurance regulators over nondepository subsidiaries and affiliates and largely defer to their reports and examinations. However, these regulatory reports and examinations were designed for a fundamentally different supervisory structure. Moreover, these regulators are simply not on site at the subsidiaries on a regular basis. In contrast to the functional regulators, our examiners are on the premises of banks and thrifts on a statutorily mandated, regular basis. Under the current regulatory regime, the bank and thrift examiners have sufficient flexibility and information to assess the risk exposure to a bank or thrift based on activities of the entire entity. Section 118 could seriously undermine this capability.

The new standards would shift our examiners' focus away from substantive supervisory concerns by forcing them to provide legalistic justifications to obtain the information they need. The standards set up needless confrontations between depository institution regulators and nonbank subsidiaries. Additionally, there may be compelling circumstances for our examiners to seek information from, or examine aspects of a subsidiary's operations that do not fall within any of the required justifications. For example, a subsidiary broker-dealer may be operating on the premises of a bank or thrift and failing to make adequate disclosures to consumers about the uninsured nature of its investment products. These activities may pose no material risk to the safe and sound operation of the institution, may not violate this Act, and may not relate to a transaction with the bank or thrift -- the requisite standards for justifying our investigating the circumstances. Yet such a failure is contrary to important and long-standing customer protection policies of our agencies and may impact the reputation risk and market perception of the institution. A different situation that could pose even greater risks arises when the broker-dealer operates off the depository institution's premises and engages in inappropriate activities with the institution's customers. In that case, the regulator of the depository institution would be denied effective tools to even make itself aware of potential problems.

The amendment's differential treatment of federally and state chartered depository institutions in bank holding company structures that own functionally regulated subsidiaries is inexplicable and has no basis in safety and soundness. The amendment would limit the authority of the OCC and OTS, the regulators of federally chartered institutions, but leaves unimpaired the supervisory authority of the states, the Federal Reserve, and the Federal Deposit Insurance Corporation ("FDIC") with respect to state banks that have functionally regulated subsidiaries and affiliates. The disparity is most apparent in a bank holding company structure with a state nonmember bank, a state member bank, a national bank, and a thrift. The states, the FDIC, and the Federal Reserve as well, may be able to use their authority as bank regulators to examine a joint subsidiary of the depository institutions, but the OCC and OTS could not. The amendment could well impede the banking agencies from working jointly on problems affecting their interrelated institutions, as we do now, because we would have different enforcement authorities.

Fewer than 10 years ago, in the face of a savings and loan and subsequent banking crisis, the Congress enacted regulatory reforms to ensure that the thrift and banking agencies had robust supervisory powers to appropriately oversee insured depository institutions and their subsidiaries and affiliates. It is particularly important for regulators of insured depository institutions to have timely information about activities and compliance by nonbank subsidiaries and affiliates so that regulators of the insured depository institution can adequately monitor transactions and enforce compliance with firewalls designed to protect the depository institution and the insurance funds from risks created by nonbank activities. This in no way detracts from the role and responsibilities of functional regulators of securities and insurance firms. It is, however, fundamental to prudent oversight of insured depository institutions.

We note that the FDIC raised similar concerns to the ones we have raised in this letter about an earlier version of this amendment and have enclosed a copy of their letter. We would be happy to discuss these important issues with you or your staff. This same letter is also being sent to Senator Sarbanes.

Sincerely,

Ellen Seidman
Director, Office of Thrift Supervision

Julie L. Williams
Acting Comptroller of the Currency

Enclosure

COVER SHEET

Center for Community Change FAX

To: Sarah Rosen, Nat'l Economic Council, The White House
Fax #: 456-2223
Subject: Opposition letter to HR 10
Date: September 23, 1998
Pages: 3, including this cover sheet.

COMMENTS:

Here is a copy of a grassroots sign-on letter that was circulated yesterday to the Senate. It was endorsed by over 800 national and local organizations, as well as by over 30 local public officials. A list of the national organization endorsers is attached.

From the desk of...

Allen J. Fishbein
General Counsel
Center for Community Change
1000 Wisconsin Avenue, NW
Washington, D.C.

202-342-0567
Fax 202-333-5462

September 21, 1998

The Honorable
United States Senate
Washington, DC 20510

Dear Senator (last name):

The undersigned organizations are writing to urge your opposition to efforts to schedule time on the Senate floor for HR 10, the "financial modernization" bill reported out by the Senate Banking Committee on September 11. In its present form, HR 10 promotes the formation of giant financial conglomerates, but contains virtually nothing to safeguard access to fundamental banking services for consumers and communities. In fact, this bill is totally opposed by virtually every community leader working to revitalize inner city neighborhoods and rural communities.

HR 10 undermines the effectiveness of the Community Reinvestment Act (CRA), the 1977 law that has served as the primary tool for directing much needed small business, small farm, and affordable housing credit into previously underserved urban and rural communities. The bill passed by the Committee makes it easier for banks to shift their assets to insurance, securities, and other affiliates not covered by the CRA. As a result, banks and thrifts will have fewer resources to lend to underserved geographies.

The Committee took a bad bill and made it worse. It deleted a requirement that banks affiliated with securities firms or insurance companies offer "lifeline" or low-cost checking accounts to low-income customers. The Committee bill also weakens extremely modest CRA provisions that were in the House-passed version of the bill, limiting the extent to which CRA would apply to new, uninsured banks created by the bill, and eliminating enforcement provisions for institutions that fail to sustain an adequate record of serving their local communities.

In short, HR 10 does nothing to modernize the laws that protect the vast majority of consumers and communities that are the most vulnerable to the disinvestment forces that the bill promises to unleash. By promoting the concentration of economic power, this bill will hurt your constituents.

The 809 community organizations signing this letter urge you to voice your opposition to this bill, ask the Senate leadership not to schedule floor time for this harmful legislation, and urge you to work with us to defeat any further consideration of HR 10.

WYOMING

The Honorable Trudy McCraken, Mayor,

NATIONAL

AFL - CIO Housing Investment Trust

Alliance to End Childhood Lead Poisoning

American Planning Association

Center for Community Change

Center for Policy Alternatives

Consumer Federation of America

Corporation for Enterprise Development

Hispanic Association on for Corporate Responsibility (HACR)

Housing Assistance Council

International Brotherhood of Teamsters

International Union of Automobile, Aerospace, and Agriculture Implement Workers / UAW

Lawyer's Committee for Civil Rights

Local Initiatives Support Corporation

NAACP

Ralph Nader

NAHRO

National Alliance to End Homelessness

National American Indian Housing Council

National Association of Affordable Housing Lenders

National Association of Community Action Agencies

National Black Chamber of Commerce

National Coalition for the Homeless

National Community Action Agencies

National Community Reinvestment Coalition

National Congress for Community Economic Development

National Council of La Raza

National Council of State Housing Agencies

National Fair Housing Alliance

National Housing Trust

National League of Cities

National Low Income Housing Coalition

National Neighborhood Coalition

National Neighbors, Inc.

National Organization for Women

National People's Action

National Puerto Rican Coalition

National Trust for Historic Preservation

Neighborhood Reinvestment Corporation

NETWORK: A National Catholic Social Justice Lobby

Rural Housing Coalition

Surface Transportation Policy Project

The Enterprise Foundation

The National Congress of Black Churches

U.S. Catholic Conference

U.S. Conference of Mayors

UNITE

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

Confidential Internal to Treasury

November 14, 1998

CONFIDENTIAL

MEMORANDUM FOR SECRETARY RUBIN
DEPUTY SECRETARY SUMMERS

FROM: Richard S. Carnell RSC
Assistant Secretary for Financial Institutions

Gregory A. Baer
Deputy Assistant Secretary for Financial Institutions Policy

SUBJECT: Rethinking Financial Modernization Legislation

Attached are three documents as background for our discussions about how to approach financial modernization legislation.

The first document (pages 2-5) responds to two questions posed by Deputy Secretary Summers: to what extent would H.R. 10 bring hedge-fund activities closer to the federal safety net; and how should recent financial turmoil, including the problems of Asian financial systems, affect our views about U.S. financial modernization legislation.

The second (pages 6-7) reviews the case for financial modernization legislation.

The third (pages 8-11) looks at possible legislative strategies in light of Senator Gramm's anticipated rise to the chairmanship of the Senate Banking Committee.

Attachments

QUESTIONS ABOUT FINANCIAL MODERNIZATION LEGISLATION

1. To what extent would H.R. 10 make it easier to bring hedge-fund activities closer to the federal safety net?

Current Law

- Banks can already expose themselves (and, indirectly, the federal safety net) to hedge funds by *lending* to those funds. But there are limits on that credit exposure.

    - Under the general limit on loans to one borrower, a national bank's total extensions of credit to any one borrower, including a hedge fund, cannot exceed 15 percent of the bank's capital (with an additional 10 percent of capital allowed if secured by certain types of readily marketable collateral).

    - Banks must hold capital against any loan, and bank examiners are supposed to ascertain whether banks have properly written down troubled loans.

    - If the hedge fund and the bank are under common control, section 23A of the Federal Reserve Act limits the bank's total extensions of credit to 10 percent of the bank's capital, and also imposes strict collateral requirements on any such lending to the fund.

- Current law strictly limits *direct investment by a bank* in a hedge fund.

    - A national bank can invest money in a hedge fund only if the hedge fund invests solely in assets of the type that the bank could invest in directly. Thus a bank could not invest in a hedge fund that holds corporate equity securities or certain types of bonds. Other restrictions apply as well: e.g., if the fund invests in futures, forwards, and options, it must do so in a manner consistent with the standards applicable to the bank's own portfolio. These restrictions would preclude banks from investing in many hedge funds.

- The Federal Reserve has, case by case, permitted *bank holding companies to invest in or manage* hedge funds, but has imposed a substantial regulatory capital penalty on any holding company that chooses to do so.

    - Specifically, the Federal Reserve has classified the activities in which hedge funds engage as "closely related to banking" and thus permissible for a bank holding company or a fund managed by such a company.

  - But the Federal Reserve, citing the reputational risks posed by managing hedge funds, has required the bank holding company -- for purposes of consolidated holding company capital requirements -- to consolidate with the holding company's own assets the assets of any hedge fund for which it serves as general partner. In effect, the holding company must hold capital against the hedge fund's assets. This capital requirement applies even when the bank holding company's own investment in the hedge fund is quite limited (e.g., 1-2 percent of the fund's total equity).

  - Moreover, if the bank holding company engages in the activity directly or through a subsidiary, any extensions of credit from affiliated banks come under section 23A's collateral requirements and 10-percent-of-capital limit.

- The Federal Reserve has not granted bank holding companies blanket authority to manage and invest in hedge funds; it requires case-by-case prior approval, which enables the Federal Reserve to act as gatekeeper and impose additional conditions as appropriate in particular cases.

H.R. 10

H.R. 10's effect on hedge fund activities is, to some degree, ambiguous because the relevant statutory language is general and has not been interpreted by regulatory agencies or the courts.[1] On balance, however, the General Counsel's office views H.R. 10 as not explicitly expanding the scope of hedge fund activities permissible for banks and bank holding companies. H.R. 10 would generally permit bank holding companies to invest in and manage hedge funds to the same extent and under the same restrictions and requirements as the Federal Reserve has imposed under current law, unless the Federal Reserve chooses to modify those conditions. Thus, unless changed by the Federal Reserve, the requirement to consolidate a hedge fund's assets with those of the bank holding company that manages it would continue to apply. But H.R. 10 would not require case-by-case prior approval for each bank holding company wishing to engage in hedge fund activities. The bill would thus eliminate the Federal Reserve's current gatekeeper role. The Federal Reserve could still seek to constrain bank holding companies' hedge fund activities through the examination process, through the periodic reports filed by bank holding companies, and through regulatory interpretation.

H.R. 10 defines a long list of activities as "financial in nature" and thus permissible for bank holding companies. Certain activities on this list -- such as merchant banking and

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[1] Unless otherwise indicated, all references in this memorandum to H.R. 10 are to the version of the bill reported by the Senate Banking Committee.

securities underwriting and dealing -- could provide some textual support for arguing that H.R. 10 would expand bank holding companies' hedge fund powers. But the General Counsel's office believes that the better reading of these terms in H.R. 10 would not encompass hedge fund activities. Moreover, because H.R. 10 continues to permit the Federal Reserve to issue regulations interpreting the Bank Holding Company Act, the Federal Reserve could prescribe restrictive definitions of the activities in question -- and thus prohibit a bank holding company from conducting hedge fund activities in the guise of merchant banking or securities underwriting or dealing.[2]

2. How should recent financial turmoil, including the problems of Asian financial systems, affect our views about U.S. financial modernization legislation?

Some Red Herrings

Banking and commerce: Opponents of allowing any common ownership of banks and nonfinancial firms will doubtless contend that the Asian experience demonstrates the risk of mixing banking and commerce. But the reality is that even the most deregulatory U.S. proposals would leave substantial walls between banking and commerce that were absent in Asia. Such proposals would, at the very least, retain section 23A, which (in addition to the collateral requirements and percentage-of-capital restrictions discussed on page 2) limits a depository institution's aggregate extensions of credit to all affiliates to 20 percent of the institution's capital. In any event, H.R. 10 would generally prohibit any affiliation between an insured depository institution and a company engaged in nonfinancial activities (except as incidental to merchant banking, in which section 23A limits would apply).

Operating subsidiary: During House floor debate over H.R. 10, some opponents of the subsidiary approach asserted that it would lead to Asian-type problems. This argument ignores the safeguards in the Treasury's proposal, notably the capital deduction requirement and the percentage-of-capital lending limits in section 23A. Moreover, consolidated financial reporting at the holding-company level would obviate any accounting differences, and leave the reputational risk the same.

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[2] Other provisions of H.R. 10 grandfather for 10 years existing activities -- including, potentially, broad hedge fund activities -- engaged in by investment banks or other companies that come under the Bank Holding Company Act after enactment of H.R. 10. Thus H.R. 10 could conceivably let a certain grandfathered set of holding companies continue engaging in a broader range of hedge fund activities during a limited time as long as they did not expand those activities.

Other Possible Lessons

Political consequences: Deregulating during a time of financial anxiety may well yield better real-world results than deregulating during a time of financial euphoria. Market participants are more likely to use sober, hard-headed judgment in assessing proposed new ventures and affiliations -- and less likely to be carried away by irrational exuberance. Hence deregulation during a time of financial anxiety runs a lesser risk of *actually creating* problems.

But deregulating during such a time runs a greater risk of being *blamed* for creating problems -- including problems that already existed or that would have arisen in any event. The issues involved are sufficiently unfamiliar to most people so that one can plausibly argue that the deregulation caused the problems, even if it actually mitigated them. Moreover, financial turmoil reminds politicians of the blame that they face if they bungle, or are thought to have bungled, deregulation. And the potential for blame increases if one can characterize the proponents of deregulation as having acted recklessly, in the face of known hazards highlighted by the financial turmoil itself. Accordingly, the points made in the preceding paragraph -- whatever their intellectual cogency -- are politically counterintuitive. Political considerations generally militate against deregulating during a time of financial anxiety.

Possible implications for GSE policy: The Asian example highlights the risk that governmental efforts to allocate credit can lead to economic inefficiencies and ultimately to losses for the lender (or the government).

The most recent Congress saw increasing attempts (through H.R. 10 and other bills) to expand the use of GSEs: e.g., to encourage lending to small businesses, agriculture, multi-family housing, and day-care center construction. Such efforts are likely to continue.

Too-big-to-fail treatment: Although H.R. 10 would have facilitated the creation of large financial conglomerates, it made no systematic effort to constrain the potential for such entities to be seen as too big to be allowed to fail, and thus as at least partially insulated from normal market discipline. Recent controversy relating to Long-Term Capital Management LP underscores the importance of giving further attention to these issues. One way to maintain market discipline would be to require the issuance of subordinated debt, which would strengthen capital markets' incentive to monitor large institutions and would help alert regulators to any deterioration in those institutions' condition.

THE CASE FOR FINANCIAL MODERNIZATION LEGISLATION

Rather than dealing with financial modernization as a single, undifferentiated concept, we focus here on the twin pillars of recent financial modernization proposals, including H.R. 10 and the Dreier-LaFalce bill: (1) allowing banks and securities underwriters to affiliate, and (2) allowing banks and insurance underwriters to affiliate.

I. The Case for Allowing Banks and Securities Firms to Affiliate

- Bank holding companies already take on and manage the risks of underwriting and dealing in a full range of securities.
  - Banks can already affiliate with securities firms, so long as underwriting and dealing in corporate securities (and other securities that a bank cannot directly underwrite and deal in) generates less than 25 percent of the securities firm's total revenue. Given the Federal Reserve liberal interpretation of this limit, almost any securities firm (e.g., Salomon/Smith Barney) can qualify.
  - When originating syndicated loans, banks take on risks similar to those of securities underwriting. And when making unsecured loans, banks arguably take on even greater risks.
  - Banks can affiliate with firms engaged in financial activities that can be even riskier than securities underwriting: e.g., commodities trading and OTC derivatives trading.
  - Thus Glass-Steagall currently fails to insulate banks from the risks of securities activities.
  - Moreover, affiliations between banks and securities firms have created few problems since bank regulators began allowing them in the 1980s.
- Glass-Steagall creates inefficiencies, inequities, and perverse incentives.
  - To create sufficient leeway under the 25-percent-of-revenue limit, bank-affiliated securities firms often run enormous matched books in government securities or rely on generating brokerage revenue.
  - Lacking such compliance options, a small bank wishing to underwrite municipal revenue bonds, for example, is likely to find that the 25 percent limit precludes it from entering the market.

II. The Case for Allowing Banks and Insurance Underwriters to Affiliate

- Affiliation with insurance companies would help diversify bank holding companies' earnings, as hard times for the banking industry would not necessarily correlate with hard times for the insurance industry.

- Life insurance underwriting has historically been a low-risk business.

- Insurance products are closely related to banking products, and customers would benefit from being able to purchase both from the same seller (although one could presumably achieve this goal by allowing affiliates of banks to sell but not underwrite insurance).

- Existing restrictions are already atrophying.

    - Banks can already sell annuities.

    - Options can be indistinguishable from insurance, and one can expect expanded bank use of derivatives to enable corporate customers to manage an increasingly broader range of risks.

    - Most large insurance companies are already in the process of purchasing thrift institutions.

        - The Federal Reserve informally questions whether the OTS, which oversees thrift holding companies, has adequate resources to assess risk at the nation's most sophisticated insurance companies. (The OTS is moving to expand its capabilities, and -- more broadly -- one should note that unitary thrift holding companies have not historically given rise to significant problems.)

WHAT SHOULD OUR LEGISLATIVE STRATEGY BE?

We face questions of legislative strategy regardless of whether or not we would prefer to see the next Congress pursue financial modernization legislation. It appears virtually certain that Chairman Leach will pursue such legislation, and it is very possible that Senator Gramm will do so as well. The question would then become whether or not we wish to be part of the process.

<u>How Should We Approach Legislation?</u>

Option 1 -- Attempt to stop legislation, emphasizing uncertainty in markets

Pro:

- Would have some chance of preventing legislation and preserving a status quo that we find tolerable, particularly if the Secretary presses the issue publicly and with Senator Gramm.

Cons:

- May well fail, given considerable industry support for a bill and two years in which to enact one.
- Would again leave us on the outside, with proponents of the bill sore at us and with the Federal Reserve probably once again in the role of dealmaker and unconstrained drafter.
- May require us to push hedge fund phobia and market turmoil farther than credibility would allow (and proponents of legislation could weaken our position by including, e.g., limits on bank-connected hedge fund activity).

Option 2 -- Work early and often with Senator Gramm to craft a bill that we find mutually acceptable

Pros:

- Senator Gramm has indicated some inclination toward our two greatest objections to H.R. 10: its rejection of the subsidiary option, and its expansion of the Federal Home Loan Bank System. That provides a reasonable starting-point for developing an acceptable bill.

- Working from the inside, we could protect the Administration's policy interests far more effectively and on a much wider range of issues.

- To the extent that we have concerns about systemic, reputational, or other risks, we could press for measures to alleviate them (e.g., a subordinated debt requirement, or restrictions on bank affiliation with hedge funds, however defined).

Cons:

- Would risk alienating Sarbanes and some other Senate Democrats (but note that Senator Dodd has a long history of working with Republican as well as Democratic Chairmen of the Banking Committee).

- Given Senator Gramm's hostility to the Community Reinvestment Act, negotiations might bog down over the CRA or put the Administration in the position of having worked on legislation that consumer and community groups strongly oppose.

Assuming We're Interested in Legislation, What Starting Point Should We Seek?

Option 1 -- Dreier-LaFalce bill (see summary below)

Pros:

- The bill is already at least arguably CRA neutral, which would help us sidestep the greatest obstacle to our working with Senator Gramm.

- The bill contains no FHLBank expansion, no unitary thrift provisions, and none of the host of provisions in H.R. 10 that aggrandize the Federal Reserve's jurisdiction at the expense of other agencies. Although the bill does not authorize new financial activities in subsidiaries, it does not prohibit them either.

- Congress would probably end up grafting various branches of H.R. 10 onto the Dreier-LaFalce tree: e.g., provisions curtailing banks' current exemption from securities broker-dealer regulation, and perhaps provisions restricting banks' insurance sales activities. But it might well be easier to modify their problematic features here -- in the context of a new bill -- than in the context of a revived H.R. 10.

Cons:

- Would mean starting from scratch and potentially reorganizing the coalition behind H.R. 10.

- H.R. 10 could still move in the House, so we may, in any event, have to pursue a House strategy of dealing with a flawed H.R. 10.

Option 2 -- H.R. 10

Pros:

- The bill has had support from all the key trade associations and seemed poised for passage not long ago.

- With Senator Gramm's support, adding a subsidiary option and omitting the FHLBank and Federal Reserve aggrandizement provisions may be just as feasible as adding the subsidiary option to the Dreier-LaFalce bill.

Cons:

- Given that H.R. 10 imposes conditions for conducting new financial activities, a decision would have to be made on whether those conditions would or would not include CRA compliance.

- Senator Gramm and others could end up splitting the difference on the provisions aggrandizing the Federal Reserve.

SUMMARY OF DREIER-LAFALCE BILL

Should Senator Gramm decide to pursue financial modernization legislation, we have reason to believe he may be inclined to work not from H.R. 10 but from a bill offered during the past Congress by Representatives Dreier (who is expected to chair the House Rules Committee during the next Congress) and LaFalce. We believe that this could be a welcome development.

In brief, the Dreier-LaFalce bill, which is only 30 pages long:

- Would repeal the anti-affiliation provisions of the Glass-Steagall Act.

- Would authorize bank holding companies to engage in any activity that the Federal Reserve determines is "financial in nature" -- a standard considerably broader than the current "closely related to banking" standard.

- Would repeal the current prohibition against bank holding companies underwriting insurance, expressly authorize them to do such underwriting, and also allow insurance companies that are part of bank holding companies to make limited nonfinancial investments under state insurance law.

- *Would do nothing else.*

    - Thus, unlike H.R. 10, the Dreier-LaFalce bill: would preserve the unitary thrift holding company; would not restrict bank insurance sales or the judicial deference accorded to the OCC; would not expand the Federal Home Loan Bank System; and would not create new "financial holding companies" or "wholesale financial institutions" (and attendant CRA controversy).

The Dreier-LaFalce bill would thus have some significant advantages -- most notably, being at least arguably CRA-neutral, as the CRA would continue to apply as currently.[3] Thus the bill could help the Administration and Senator Gramm to finesse the most potentially divisive issue between them.

The Dreier-LaFalce bill could probably not emerge from Congress in its current lean condition. Securities firms and the Securities and Exchange Commission would certainly wish to include H.R. 10's limitations on the bank broker-dealer exemption, and insurance interests would also press for restrictions on bank insurance sales. Still, the Dreier-LaFalce bill would probably not collect as much baggage objectionable to us as H.R. 10 already contains -- particularly if we were working with Senator Gramm.

cc: Jerry Hawke
Michael Froman
Gary Gensler, Ed Knight; Linda Robertson
Roger Anderson; Michael Barr; Karen Kornbluh; Sheryl Sandberg; Marne Levine

---

[3] H.R. 10 would have explicitly required a satisfactory CRA rating as a prerequisite for the conduct of any new financial activity. Under current law (and the Dreier-LaFalce bill), the agencies consider a banking organization's CRA record in any depository institution acquisition or merger, but do not consider it when acting on applications to engage in nonbanking activities.

3-2-99

THE WHITE HOUSE
WASHINGTON

March 1, 1999

Mr. President:

This Rubin/Sperling/Reed/Stein memo asks you to approve a letter to Senate Banking Committee Chairman Gramm -- from either you or John Podesta -- that threatens a veto of the financial services modernization bill scheduled for mark-up before that committee on Thursday.

The memo details why your advisers believe Gramm's bill would weaken the Community Reinvestment Act (CRA); erode the Administration's role in financial services policymaking; weaken consumer protections; and permit unwarranted leeway for banks to merge with commercial firms. They think a veto threat now will aid a better bill being advanced in the House by Reps. Leach/LaFalce; underscore the CRA's importance; help rally/unify Senate Democrats; and highlight your opposition to a bad bill *and* your support of a good one.

Chances for overall passage appear stronger this year than last, when similar legislation (H.R. 10) ran aground in the Senate over CRA and other issues, including Administration opposition. The Leach/LaFalce version is generally acceptable; it allows affiliations among different types of financial services firms without undercutting the CRA or the Administration's policymaking authority. Senator Sarbanes is gathering support for a similar Senate alternative and requested a veto letter.

Approve ✓ Disapprove ___ Discuss ___

Phil Caplan
Sean Maloney

Gene
How to respond?
Is any of this possible
Bc

RAINBOW/PUSH COALITION

National Office
930 East 50th Street
Chicago, IL 60615
Phone: 773-373-3366
Fax: 773-373-3571

Washington, DC Bureau
1002 Wisconsin Ave., NW
Washington, DC 20007
Phone: 202-333-5270
Fax: 202-728-1192

New York Bureau
330 West 42nd St.
Suite 1511
New York, NY 10036
Phone: 212-425-7874
Fax: 212-968-1412

Los Angeles Bureau
12021 Wilshire Blvd.
Suite 700
Los Angeles, CA 90025
Phone: 310-889-1111
Fax: 310-471-1453

Detroit Bureau
st National Building
Woodard Ave.
Suite 1433
Detroit, MI 48226
Phone: 313-963-9005
Fax: 313-963-9012

copied
Sperling
Podesta

October 28, 1999

10-28-99

The Honorable William Jefferson Clinton
President of the United States of America
The White House
Washington, D.C. 20500

Dear President Clinton:

I pressed hard for a Financial Services Modernization bill that took a strong stand on the Community Reinvestment Act (CRA). When it became clear that the final bill would assure that CRA remains vital and relevant in the new financial landscape, I was quick to praise it and I still do.

However, when I look at some of the finer details of the bill, I believe that changes are still needed to address the ominous language of the "sunshine" provisions. While I support the notion that community organizations should be held accountable, I believe the detailed reporting language will cast a pall over CRA by local community groups. Additionally, I am concerned that the real reason for these provisions is to collect the necessary data for future attacks on CRA. These provisions implicitly support the premise that community groups are engaged in extortion and fraud regarding CRA. These reporting and penalties will have a chilling effect on groups' efforts to highlight weaknesses in bank performance as well as their efforts to forge partnerships with lenders.

I believe that in addition to the significant changes already made, two modest additional changes are necessary to restore equilibrium to CRA. These changes would in no way adversely affect the bill and they should be supported by the banking industry.

First, under the CRA Sunshine Requirements, I would like to see the proposed new Sec. 48 (c)(3) of the FDI Act elimina[illegible] information requested under these reporting requirements is too highly detailed and burdensome, particularly for small community groups who do not maintain information in this format.

Second, efforts were made in the legislative drafting to narrow the scope of activity defined as a "CRA agreement," limiting it to activity relating to bank applications and examinations. I believe that the proposed new Sec. 48 (e)(1)(B)(ii) should eliminate references to individuals and organizations that have "discussed or otherwise contacted the institution" concerning CRA. These phrases case an extremely broad net and would cover situations where a bank – even one with no application pending or a scheduled CRA exam – approached a community group about establishing a partnership that might be counted as part of its CRA record. Without a change, community groups will rightly fear that even the slightest criticism of bank performance will ensnare them in a federal regulatory review.

Lastly, I understand that several privacy groups are unhappy with the bill. While some progress has been made, more needs to be done.

We are in the final throes of this process, and I need your support for these changes to the bill. I believe that with these adjustments we can create a stronger piece of legislation that serves both the financial industry and their local community partners.

Sincerely,

Jesse L. Jackson

Rev. Jesse L. Jackson, Sr.

THE WHITE HOUSE

WASHINGTON

March 1, 1999

MEMORANDUM FOR THE PRESIDENT

CC: THE VICE PRESIDENT

FROM: ROBERT RUBIN
GENE SPERLING
BRUCE REED
LARRY STEIN

SUBJECT: Financial Services Legislation

ACTION-FORCING EVENT: On March 4, the House and Senate Banking Committees are both scheduled to mark up major financial services legislation. The House bill, developed by Chairman Leach and Ranking Democrat LaFalce, is generally acceptable. But the Senate bill being developed by Chairman Gramm is seriously flawed. While we expect to see another draft of the Gramm bill later today, the most recent draft would remove outmoded barriers to affiliations among different types of financial services firms, but it would also: (1) weaken the effect of the Community Reinvestment Act (CRA); (2) erode the national bank charter and the Administration's role in financial services policymaking; (3) provide inadequate consumer protections; and (4) provide increased leeway for affiliations between banks and nonfinancial firms.

RECOMMENDED ACTION: That you or John Podesta on your behalf sign the attached letter stating that you would veto the Senate bill in its current form (Attachment A).

Agree ____ Disagree ____ Discuss ____

BACKGROUND: Both Houses of Congress are currently considering legislation to permit the full range of financial services firms—including banks, securities firms, and insurance companies—to affiliate with one another. This memorandum describes the current status of such "financial modernization" legislation and outlines a strategy for countering the most objectionable features of the Senate bill.

Attachment B provides a more detailed discussion of the issues in question.

In General

The 1933 Glass-Steagall Act generally prohibits affiliation between banks and securities firms. The Bank Holding Company Act of 1956 generally prohibits affiliation between banks and insurance companies. Large financial services firms strongly support removing these barriers to affiliation, although consumer and community groups generally see little benefit in such changes.

Repealing barriers to affiliation among financial services firms has the potential for giving consumers greater choice and lower costs. However desirable the general goal of financial modernization, it does not warrant accepting a seriously flawed bill. Financial modernization is already occurring in the marketplace, and will continue even without legislation.

Over the years, efforts to enact financial modernization legislation have repeatedly failed in the face of infighting among different types of financial services firms. By the end of the last Congress, however, a financial modernization bill known as H.R. 10 had received broad support from the banking, securities, and insurance industries. The bill passed the House but died on the Senate floor for two reasons. First, Senators Gramm and Shelby opposed what they characterized as an expansion of the Community Reinvestment Act. Second, the Administration objected that the bill would have undercut its role in financial services policymaking and had the effect of weakening CRA.

Status of Legislation

As this Congress turns to financial modernization legislation, the inter-industry consensus on the need for such legislation remains intact. Both the Banking Committees are scheduled to mark up financial modernization bills on March 4. Given that early start and the momentum for some sort of legislation, the prospects for passage of legislation are stronger than in the last Congress, though still uncertain.

- *House.* The Leach-LaFalce bill has been developing along very constructive lines, and we anticipate that it will merit our support. As discussed in Attachment B, the bill accomplishes the basic work of financial modernization—allowing affiliations among different types of financial services firms—and does so consistent with our views on the Community Reinvestment Act, banking structure, and other issues. The House Leadership is by all accounts committed to moving some sort of financial modernization bill. The House Commerce Committee, however, may seek changes that could be unacceptable.

- *Senate.* Chairman Gramm is scheduled to release a committee print on March 1. As further described in Attachment B, Gramm's recent draft bill runs counter to our views on CRA, banking structure, consumer protection and promoting a separation between depository institutions and commercial firms. Senator Sarbanes, the Ranking Democrat, is working with the Treasury to unite Banking Committee Democrats behind an alternative bill that will have much in common with the Leach-LaFalce bill. The Committee is likely to approve the Gramm bill on a straight party-line vote.

CRA: The current version of the Leach-LaFalce compromise requires a bank to have and maintain a satisfactory CRA record in order to engage in newly authorized non-banking activities—a requirement not included in the Administration's 1997 bill, but which we have since argued is essential to maintaining the vitality of CRA. The draft Gramm bill contains no such "have and maintain" requirement, and includes two amendments that would seriously undermine CRA.

Some House Democrats may seek to go on the offensive by proposing to expand CRA. For example, Representative LaFalce may offer an amendment to make explicit that public comment on an institution's CRA record must be considered in applications for newly authorized activities, an amendment we could support. Last year, Representative LaFalce introduced an amendment requiring financial institutions to report on their progress in meeting publicly announced "commitments" under CRA; currently no such reporting occurs. Other House committee Democrats may offer amendments to extend the reach of CRA to insurance companies and securities firms.

Near-Term Strategy

Our near-term goal is to assist Leach and LaFalce in moving their bill forward, while doing everything possible to block the Gramm bill. This strategy has four advantages. First, we would help advance the better of the two bills. Second, we would take a strong stand against weakening CRA. Third, we would help unite Senate Democrats against the Gramm bill. Fourth, we would be taking a visible stand against a bad "financial modernization" bill, while simultaneously supporting a good bill.

To further this strategy, we recommend that you --as requested by Senator Sarbanes -- or John Podesta on your behalf send a short letter stating that you would veto the Gramm bill if it were presented to you in its current form. The proposed letter would cite two reasons from last Congress: The bill's weakening of the effect of CRA, and the bill's flawed banking structure issues. It would also cite two new reasons: the bill's inadequate consumer protections (notably the failure to provide adequate investor-protection safeguards on the sale of securities to bank customers), and its extensive expansion of non-financial firms' ability to affiliate with banks.

Secretary Rubin would send a letter setting forth a fuller explanation of our reasons for opposing the Gramm bill. He would also send a letter supporting the Leach-LaFalce bill.

Finally, your advisors are discussing the merits of various CRA proposals and how we should respond to amendments that would enhance enforcement of CRA, such as the LaFalce amendments. Some think that supporting something along these lines could strengthen our hand in negotiations later on; moreover, as we provide the industry with new opportunities, they argue, we should insist on some new responsibilities. However, some of these amendments would present an uncomfortable vote for moderate Democrats, have slim prospects for passage, and could possibly jeopardize the CRA provisions already in the House bill.

Attachments

ATTACHMENT A: PROPOSED LETTER TO CHAIRMAN GRAMM

Dear Mr. Chairman:

This Administration has been a strong proponent of financial legislation that would reduce costs and increase access to financial services for consumers, businesses and communities. Nevertheless, we cannot support the "Financial Services Modernization Act of 1999" now pending before your Committee.

In its current form, the bill would undermine the effectiveness of the Community Reinvestment Act, a law that has helped to build homes, create jobs, and restore hope in communities across America. The CRA is working, and we must preserve its vitality as we write the financial constitution for the 21st Century. The bill would deny financial services firms the freedom to organize themselves in the way that best serves their customers, and prohibit a structure with proven advantages for safety and soundness. The bill would also provide inadequate consumer protections. Finally, the bill would expand the ability of depository institutions and non-financial firms to affiliate, at a time when experience around the world counsels caution in this area.

The President [I] agree[s] with you that reform of the laws governing our nation's financial services industry would promote the public interest. However, he [I] will veto the bill if it is presented to him [me] in its current form.

Sincerely,

ATTACHMENT B: KEY ISSUES

1. Community Reinvestment Act

Current Law. CRA requires a bank to serve the convenience and needs of all communities in which it operates. Although banks are examined periodically for CRA compliance, enforcement comes only when a bank files an application to merge with another bank or open a new branch. The regulator must then consider the bank's CRA record in evaluating the bank's application, and the public has an opportunity to comment on the application. A bank's CRA record is not *currently* scrutinized in connection with applications to affiliate with non-banking companies.

Early in your Administration, and at your request, the banking regulators revised the regulations implementing CRA to focus on performance, not paperwork. They now base CRA ratings on a three-pronged test: lending, services, and investments. Regulators also revised and streamlined the examination process, particularly for smaller institutions.

Conditioning Authority to Conduct New Non-banking Activities on Banks Having a Satisfactory CRA Record. We have argued that financial modernization legislation must preserve the relevance of CRA for the 21st century, and must not weaken the effect of CRA. CRA's relevance should be maintained by conditioning authority to conduct new non-banking activities on banks having a satisfactory CRA record. Although the Administration's 1997 bill did not impose a link between CRA and non-banking activities, we have insisted in this Congress that a bank both *have* and *maintain* an adequate CRA record as a condition of engaging in newly authorized non-bank activities. This would provide additional means for enforcing existing CRA obligations. Noncompliance would result in submission of a compliance plan (and ultimately, albeit unlikely, forced divestiture).

The Leach-LaFalce compromise requires the bank to have *and* maintain a satisfactory CRA rating, though amendments (including by Leach himself) are possible. Secretary Rubin has testified that if we wish to preserve the relevance of CRA, at a time when the relative importance of bank mergers may decline and non-bank financial activities are becoming increasingly important, authority to engage in newly authorized non-bank financial activities must be conditioned on satisfactory CRA performance.

Gramm's draft bill imposed no such condition. Gramm views such a requirement as an unprecedented expansion of CRA to non-bank activities, and has told the Secretary that he would prefer no bill to a bill with such a condition. We have argued, though, that the financial services system of the future may include rather fewer banking applications (and therefore fewer opportunities for enforcement of CRA) and more non-banking activities (where an ongoing requirement of a satisfactory CRA record would be a meaningful incentive for compliance). Thus a bill that is silent on CRA (and thus supposedly neutral) would, in our view, tend to weaken the effect of CRA, and we would oppose such a bill.

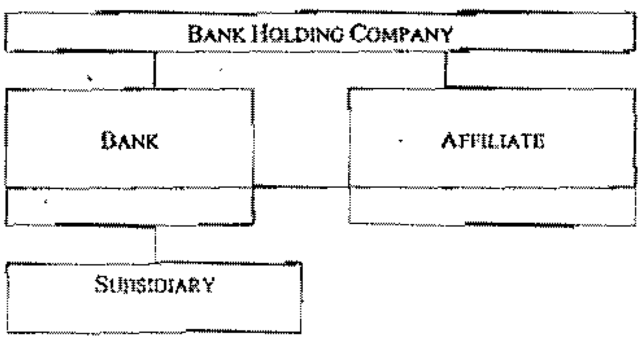
Gramm's Safe Harbor Amendment. Gramm has proposed a safe harbor for applications now subject to CRA. A satisfactory CRA rating at a bank's most recent examination would conclusively establish the bank's CRA performance, unless a public comment provides substantial verifiable information to the contrary. A regulatory agency could not review the bank's CRA record unless there were an adverse public comment meeting the test—even if the previous examination were old or otherwise stale. And Gramm would create a rebuttable presumption favoring approval of the application. In so doing, he would place a significant burden of proof on consumer and community organizations that generally have less access than the bank to relevant information. He would also, in effect, force community groups to stretch their limited resources to comment on many examinations, instead of focusing those resources on major applications (e.g., for mergers or acquisitions). Secretary Rubin has testified that such a safe harbor would tend to eviscerate the effectiveness of CRA, and the Administration has repeatedly threatened vetoes of bills containing safe harbors provisions.

Gramm's Anti-extortion Amendment. Gramm has also proposed a so-called "anti-extortion" provision which may be dropped from the bill. We strongly oppose extortion. Yet laws punishing extortion, bribery, and false statements already protect against misuse of the CRA process. Gramm's broad and vague proposal would criminalize normal, legitimate arms length transactions and cooperation between banks and community groups (e.g., bank grants to support community groups' home ownership counseling programs)—the very sort of activity CRA seeks to foster.

It is important to note that if we should end up opposing a bill, for whatever reason, CRA will be the issue best able to unite Democrats behind us.

2. Allowing Firms the Choice of Operating through Subsidiaries as Well as Affiliates.

Since 1995, the Treasury has advocated giving financial services firms that include banks the option of conducting newly authorized financial activities (e.g., securities underwriting) in through a subsidiary or an affiliate.



The Fed, by contrast, has insisted that new activities be allowed only in Fed-regulated affiliates.

We have emphasized four points to Members of Congress:

- Absent a demonstrable public interest to the contrary, financial services firms should have the same freedom as other businesses to organize themselves in the way that best serves their customers.

- The subsidiary approach has strong safety and soundness advantages. If the subsidiary prospers and the bank falters, the bank's interest in the subsidiary can be sold to help replenish the bank's capital—or reduce any loss to the FDIC. Yet if the bank prospers and the subsidiary falters, the bank faces no greater risk than if an affiliate faltered. Four past and present Chairmen of the FDIC have strongly agreed with this point, arguing that the subsidiary offers better protection to the FDIC and the taxpayer.

- Banks with new financial activities in subsidiaries will have more earning assets, and thus will be stronger and better able to serve their communities under CRA.

- The subsidiary/affiliate option would also help preserve the current balance among the regulatory agencies by giving both Treasury/OCC and the Fed a role in supervising new financial activities. In so doing, it would help safeguard the role of the President and the Executive Branch in financial services policy making.

These efforts appear to be bearing fruit. On the House side, the Leach/ LaFalce compromise includes the subsidiary option, and permits subsidiaries to conduct all financial activities except insurance underwriting. On the Senate side, Chairman Gramm's discussion draft would allow the subsidiary option only to banks with less than $1 billion in assets—an approach that Secretary Rubin has labeled a non-starter. We understand, however, that several Banking Committee Republicans (Bennett, Grams, Shelby) strongly support our position (and may well be joined by Hagel and Mack). Among the Democrats, Senator Sarbanes, formerly a critic of the subsidiary option, will include the Leach-LaFalce subsidiary in the Democratic substitute.

3. Consumer Protection

We believe that financial modernization legislation should contain appropriate consumer protections, including safeguards relating to the sale of non-banking products to bank customers (e.g., suitability and disclosure requirements). The Leach-LaFalce bill contains such protections. Yet the Gramm bill, although it would significantly expand the potential for affiliations between banks and securities firms, fails to provide adequate investor protections in connection with the sale of securities to bank customers.

4. Banking and Commerce

Considerable controversy has arisen recently over proposals to "mix banking and commerce", i.e., to allow depository institutions to affiliate with non-financial firms.

Secretary Rubin has expressed serious reservations about allowing affiliations of depository institutions and non-financial firms. Experience in Asia raises concerns that mixing banking and commerce can lead to inefficient allocation of resources and exposure of the banking system to risk. Chairman Greenspan has expressed similar sentiments, arguing that we should assess the effect of allowing full affiliation among financial firms before allowing affiliations with non-financial firms. Senator Sarbanes strongly opposes mixing banking and commerce. Assistance on the subsidiary issue was conditioned on our support on this issue. Chairman Leach also opposes mixing banking and commerce.

The draft Gramm bill proposed a significant expansion of banking and commerce. For example, under the Gramm draft, a large banking organization could own a mid-sized commercial firm, and a large commercial firm could own a small bank. Also, any commercial firm would be permitted to own a savings association (thrift) of any size, as under the current "unitary thrift holding company" law.

The Leach-LaFalce bill contains what may be an acceptable compromise. New commercial affiliations would not be permitted, and the unitary thrift holding company would be prohibited going forward (with existing ownership grandfathered). The compromise depends, though, on a slightly broader definition of permissible financial activities, which we will need to negotiate.

S 900 -- 05/03/99
OMB Home

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

STATEMENT OF ADMINISTRATION POLICY
(THIS STATEMENT HAS BEEN COORDINATED BY OMB WITH THE CONCERNED AGENCIES.)

May 3, 1999
(Senate)

S. 900 - Financial Services Modernization Act of 1999 (Gramm (R) TX)

The Administration strongly opposes S. 900, which would revise laws governing the financial services industry. This Administration has been a strong proponent of financial modernization legislation that would best serve the interests of consumers, businesses, and communities, while protecting the safety and soundness of our financial system. Consequently, it supports the bill's repeal of the Glass-Steagall Act's prohibition on banks affiliating with securities firms and of the Bank Holding Company Act's prohibitions on insurance underwriting. Nevertheless, because of crucial flaws in the bill, the President has stated that, if the bill were presented to him in its current form, he would veto it.

In its current form, the bill would undermine the effectiveness of the Community Reinvestment Act (CRA), a law that has helped to build homes and create jobs by encouraging banks to serve creditworthy borrowers throughout the communities they serve. The bill fails to require that banks seeking to conduct new financial activities achieve and maintain a satisfactory CRA record. In addition, the bill's "safe harbor" provision would amend current law to effectively shield financial institutions from public comment on banking applications that they file with Federal regulators. The CRA exemption for banks with less than $100 million in assets would repeal CRA for approximately 4,000 banks and thrifts that banking agency rules already exempt from CRA paperwork reporting burdens. In all, these limitations constitute an assault upon CRA and are unacceptable.

The bill would unjustifiably deny financial services firms holding 99 percent of national bank assets the choice of conducting new financial activities through subsidiaries, forcing them to conduct those activities exclusively through bank holding company affiliates. Thus the bill largely prohibits a structure with proven advantages for safety and soundness, effectively denying many financial services firms the freedom to organize themselves in the way that best serves their customers.

The bill would also inadequately inform and protect consumers under the new system of financial products it authorizes. If Congress is to authorize large, complex organizations to offer a wide range of financial products, then consumers should be guaranteed appropriate disclosures and other protections.

The bill would dramatically expand the ability of depository institutions and nonfinancial firms to affiliate. The Administration has serious concerns about mixing banking and commercial activity under any circumstances, and these concerns are heightened by the financial crises affecting other countries over the past few years.

The Administration also opposes the bill's piecemeal modification of the Federal Home Loan Bank System. The Administration believes that the System must focus more on

THE WHITE HOUSE

WASHINGTON

May 3, 1999

FINANCIAL PRIVACY AND CONSUMER PROTECTION EVENT

DATE:	May 4, 1999
TIME:	2:00 – 3:15 p.m.
LOCATION:	Room 450
FROM:	Gene Sperling

I. PURPOSE

Over the past few years, new technology and increased competition have truly revolutionized the financial services industry. By and large, these changes have been very good for consumers. But technology and increased competition have also created new challenges. To prepare for the 21st Century economy, we must update our privacy and consumer protection laws for our rapidly changing financial marketplace. At this event, you will outline the administrative steps we are taking, and the legislative proposals we support to give all Americans the tools and confidence they need to participate in financial activities in our thriving but highly complex 21st Century economy.

The initiative contains both administrative and legislative proposals in five areas: (1) financial privacy; (2) disclosure/right-to-know (in credit card, banking, and other services); (3) protection against fraud; (4) expanding access to financial services; and (5) consumer financial education.

II. BACKGROUND

There is little prospect that a package of consumer financial protection initiatives will move as a whole in this Congress. However, pieces of the package could be considered in the context of other financial legislation. This week Financial Modernization is on the floor of the Senate and Bankruptcy is on the floor of the House. This package will give Democrats numerous consumer protection proposals that they can advance that will earn enthusiastic Administration support. The list does not include all the Democratic proposals that are currently pending before Congress, but a significant proportion of those and all that we think are justified on policy grounds.

Some Republicans will argue that you are signaling your desire to kill Bankruptcy and Financial Modernization legislation by offering proposals that would be unacceptable to those bills' proponents. However, in Financial Modernization, the Administration has indicated strong support for the bipartisan bill reported out of the House Banking Committee and the Democratic bill offered in the Senate. Both those bills contained only modest privacy proposals, far less aggressive than those that we support here today. In Bankruptcy, last year we supported the Senate-passed bill that contained credit card, minimum payment disclosure requirements, but only a small fraction of the proposals that we support here today. **In both bills, the key for your Administration has been balance.** We do not insist on a wish list -- just that the bills provide some appropriate consumer protections.

Finally, this event has been rescheduled numerous times because of the turmoil of recent events. As a result, preliminary drafts of the proposals have been widely distributed. In general, consumer groups are very pleased, although they always would like more. Industry's criticism will be very muted. They may even say kind things about many aspects of the initiative. They have indicated their desire to work with the Administration on these issues/

III. PARTICIPANTS

Brief Participants
John Podesta
Secretary Rubin
Gene Sperling
Sarah Rosen
Larry Stein
Lowell Weiss

Event Participants
The President
The First Lady
Secretary Rubin
Mari Frank, the real person
Senator Sarbanes (seated on podium – not speaking)
Representative LaFalce (seated on podium – not speaking)

IV. SEQUENCE OF EVENTS

- **YOU** will be briefed by your advisors in the Oval Office.
- **YOU** proceed to the OEOB.
- **YOU** meet briefly with Members and Ms. Mari Frank and enter Room 450.
- The First Lady makes brief remarks and introduces Secretary Rubin.
- Secretary Rubin will make brief remarks and introduce Ms. Mari Frank.
- Ms. Frank will make brief remarks and introduce **YOU**.
- **YOU** will make your speech.

Senator Sarbanes and Representative LaFalce (the ranking members on the Senate and House Banking Committees) will be seated on the podium with you, but they will not make remarks. Other members who have supported pending bills on these topics in Congress will be in the audience.

V. PRESS COVERAGE

Open Press

VI. REMARKS

To be provided by speechwriting.

VII. ATTACHEMENTS

- Draft 2-page press background paper

DRAFT

THE CLINTON-GORE PLAN FOR
FINANCIAL PRIVACY AND CONSUMER PROTECTION IN THE 21st CENTURY
May 03, 1999 -- draft
DETAILED PROPOSAL SUMMARY

INTRODUCTION

Technology and competition in financial services give Americans more complex choices than ever before. Innovations in the financial marketplace offer millions of consumers new, ever increasing choices for investing their savings and obtaining credit. But new products have brought new risks and new abusive practices. We must update our consumer protection laws to give consumers the power, information and protection they need to profit from our 21st Century financial system.

Members of Congress, including Ranking Members Sarbanes and LaFalce, have sponsored important legislation to modernize our consumer financial protection laws. We applaud their leadership and look forward to working with Congress on a consumer protection agenda.

Set forth below is a series of actions that the Clinton Administration believes should be part of this agenda. The list is not exhaustive, and we will continue to look for constructive ideas in these and other areas. Among the issues deserving further scrutiny are lending practices such as "pay day" loans (short-term loans which can carry interest rates of 400%) and bank check processing practices that may be designed to maximize bounced check fees. We will work with the states and the FTC wherever possible. Secretary Cuomo is making important efforts to address abusive mortgage lending practices.

PROTECT FINANCIAL PRIVACY

Require institutions to inform consumers of plans to share or sell their financial information, and give the consumer the power to stop it. Although consumers put great value on the privacy of their financial records, our laws have not caught up to technological developments that make it possible and potentially profitable for companies to share financial data in new ways. Current law does provide some important privacy protections: for example, the Fair Credit Reporting Act (FCRA) requires a form of notice and opt-out before certain information about consumers (e.g., information provided on an account application) can be shared. But there are no limits on the sharing of information about consumers' transactions (e.g., account balances, who they write checks to) within a financial conglomerate, or even on the sale of that information to a third party. We support legislation to give consumers control over the use and sharing of all their financial information.

Impose special restrictions on any sharing of medical information within a financial conglomerate. Our greatest privacy concerns involve medical information. Yet, cross-industry mergers and consolidation have given banks unprecedented access to consumers' medical records. We support legislation requiring that medical information, such as that gathered from life insurance records, not be shared within financial services conglomerates (e.g., between banking and insurance affiliates), except for narrowly defined purposes. Consumers who undergo physical exams to obtain insurance, for example, should not have to fear that the information will be used to lower their credit card limits or deny them mortgages.

Give bank regulators the authority they need to ensure compliance with existing privacy protections. Currently, bank regulators may not examine for compliance with existing privacy protections, but must wait for a consumer complaint. Congress should give regulators broader authority to monitor compliance.

Publicize best practices in the privacy area. Even in the absence of legislation, many responsible banks have begun posting their privacy practices on the Internet and otherwise informing customers about how their data is handled. The Office of Thrift Supervision has issued guidance in this area. Today, the Office of the Comptroller of the Currency is publishing best practices in this area, so that additional institutions can be encouraged to inform their customers and do so in the most effective way possible.

Coordinate privacy policy in the financial and other sectors. We must ensure that a proper balance is struck between information flows and personal privacy, for financial services and more broadly. To coordinate the Administration's privacy policy, we have created the new position of Chief Counselor for Privacy, in the Office of Management and Budget.

EXPANDING THE CONSUMER'S RIGHT TO KNOW

Credit Card Disclosures

Prevent Misleading Credit Card Marketing of "Teaser" Rates. Consumers frequently complain that they did not understand marketing materials on credit card interest rates and are shocked when rates skyrocket, whether because a "teaser" rate expired or they had a minor late payment. Some consumers are misled by mailings that promote a "low 3.9% initial rate" but fail to disclose as prominently that the rate doubles or triples in six months or with a single late payment. We support legislation requiring "teaser" rates for credit cards to be accompanied by equally prominent disclosure of the expiration date of the initial rate and the eventual APR.

Require Credit Card Minimum Payment Disclosures. In recent years, credit cards lenders have lowered minimum payments. Many consumers still assume, however, that, as with a monthly mortgage payment, repeated payment will eventually retire the debt. In reality, low minimum payment requirements and high interest rates often means that borrowers make little, if any, headway. We support legislation requiring clear and conspicuous notice of how long and how costly repayment would be if a consumer makes only the minimum payment.

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Disclosure of Late Payment Fees. It can be hard to tell from a credit statement whether and when a late payment fee (in addition to interest on the unpaid balance) will be assessed. We support legislation requiring monthly statements to display prominently the date that payment is due, together with any late payment fee.

Disclosure of Security Interests. Increasingly, creditors take security interests in goods purchased on credit. While consumers should expect to lose such goods if they fail to repay, they ought to know if they are granting a lien. For goods with little resale value, such liens may be taken as a collection technique or to encourage reaffirmation of the debt if the consumer goes into bankruptcy. We support legislation requiring effective notice of liens taken.

Disclosure of Interest Rates and Fees on Credit Advances Through Third-Party Checks. Credit cards offer some card holders "convenience" checks that allow them to write checks against their credit account in places where credit cards are not honored. But card holders may not understand that rates and charges are typically higher than for their credit card. Currently, these charges are explained only in initial disclosures but not at the time that the checks are sent to the consumer. That law should be changed.

Apply Disclosure Rules to Internet Credit Card Solicitations. More and more, credit cards are marketed to consumers on the Internet, but current law does not require the same complete disclosures as apply to direct mail solicitations. We support legislation requiring that all Internet credit card solicitations include clear and conspicuous disclosure of the card's terms and conditions, updated regularly to reflect current terms and costs.

Bank Disclosures

Provide Enforcement "Teeth" for Rules on Bank Sale of Non-Deposit Products. Increasingly, consumers buy securities, mutual funds, annuities, insurance on bank premises. Although none of these non-bank products are insured, studies have shown that many customers believe that these products are FDIC-insured or that the bank would protect them from loss. Under current bank regulator guidelines, banks that sell non-deposit products must disclosure that those products are not federally insured and limit their practices to avoid such confusion, for example by selling these products at a space physically separate from where banking transactions occur. However, a violation of these guidelines brings no penalties. We call on the banking regulators to adopt regulations that will be fully enforceable by civil money penalties and other sanctions.

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Require Disclosure and Other Protection for Rent-to-Own (RTO). The attraction of obtaining a TV, refrigerator, or living room furniture with little down has spurred the rapid growth of firms offering to rent products with an option to buy. But an RTO firm can sell a customer a used product that looks new, and the consumer can pay many times the value of the product. The FTC is nearing completion of a study of the RTO industry. We look forward to its recommendations, and expect to support a legislative response. Adequate consumer protections, including disclosure so consumers can compare the cost of RTO to other alternatives, should be required. In addition, we will work with states to ensure that any federal rules do not interfere with or preempt state consumer protection efforts, including regulation of RTO under state credit sales and usury laws.

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Require ATMs to provide clear and conspicuous disclosures of surcharges on the machine and terminal screen. When customers use an ATM, the operator of the machine may impose a sizeable surcharge. Accordingly, most consumers shop around to avoid ATM fees or pay less. A conspicuous posting of the amount of any surcharge allows customers to walk past higher priced machines, or at least to begin the transaction with their eyes open. While ATM networks generally require members to post fee notices on the machine, a recent survey shows that nearly 25 percent of machines had either no posting or an inaccurate one. We support legislation requiring ATM owners to post a clear and conspicuous notice on the machine as well as on-screen, and subjecting ATM owners to sanctions for failure to make the mandated disclosures.

Mortgages

Require Enhanced Disclosure for Mortgage and Settlement Services and Stem Abusive Practices. In July 1998, the Federal Reserve Board and the Department of Housing and Urban Development released a Congressionally mandated study of how best to streamline the statutory disclosure requirements for mortgage loans and settlement services, with the goal of simplifying and improving the quality of information provided to consumers to enhance their ability to shop and increase competition. The report calls for a series of statutory reforms to the Real Estate Settlement Procedures Act and the Truth in Lending Act to make the information provided to consumers more reliable, more timely, and more helpful in comparison shopping for all the services required to finance a home. Congress should adopt the report's recommendations. For example, the required annual percentage rate disclosure should include all costs the consumer is required to pay in order to receive credit, instead of the patchwork of costs currently disclosed. Creditors should be required to provide firm and reliable rate, fee, and closing cost information, and disclosures should be made early in the application process, before creditors impose substantial fees. It also is important to make sure that information provided to consumers is readily understandable.

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PREVENT FRAUD AND ABUSIVE PRACTICES

Devote Law Enforcement and Agency Resources to Financial Fraud.

"Identity Theft" Enforcement Initiative. Identify theft is the use of another's individual identifying information to commit an offense -- for example, using another's social security number to apply for a credit card.) Once, one had to forge or steal documents to impersonate another, but now one can easily use your identifiers to impersonate you over the phone or Internet. This type of crime is growing rapidly [insert numbers]. Last year, Congress enacted new laws barring the use of another's identifying information. The Secret Service, in coordination with the Justice Department and regulatory agencies, will launch a vigorous identity theft enforcement and prevention strategy that includes referral of cases among federal, state and local law enforcement; developing a public-private partnership to educate consumers on how to protect themselves; and proposing sentencing enhancements. They will cooperate with the American Bankers Association and others in the banking industry that have worked to combat this problem.

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Complaint Center, augment training for law enforcement on how to recognize and prosecute Internet securities fraud and continue its efforts to educate investors about the risk and rewards of investing over the Internet.

Internet Fraud Initiative: Federal, state and local law enforcement officials and regulatory agencies are receiving a growing number of complaints from consumers about Internet fraud. Many of the same features of the Internet that make it a powerful tool for legitimate e-commerce (global reach, instant and often anonymous communications, ability to reach millions of consumers) -- also make it attractive for fraud schemes. The Internet Fraud Initiative will crack down on Internet fraud by, for example, stepping up training for federal, state, and local prosecutors and agents; developing information on the nature and scope of Internet fraud; and keeping the public better informed about current fraud schemes and how to handle them. The initiative will also help coordinate the efforts of federal (Department of Justice, the FBI, the U.S. Secret Service, the Postal Inspection Service, the Federal Trade Commission, and the Securities and Exchange Commission), state and local law enforcement agencies.

Criminalize "Pretext Calling." There are widespread reports of private investigators and data brokers tricking financial institutions into providing confidential customer information. Along with the banking industry, we support legislation that would criminalize this practice and protect the privacy and security of consumer financial information.

Fully Implement FTC-HELP and Consumer Sentinel. The Year 2000 will be the first full year of operation for FTC's toll-free consumer hotline, part of the Commission's Consumer Response Center. The hotline will give consumers fast and easy access to information they need to protect themselves -- from tips about credit and debt collection to advice on how to avoid becoming a victim of fraud. Complaints to the hotline become part of the Consumer Sentinel, the FTC's fraud database, which is shared only with other law enforcers in the U.S. and Canada. By 2000, the Consumer Sentinel database is expected to be a primary tool in the fight against consumer fraud. The President's FY2000 budget funds Consumer Sentinel.

Improve Consumer Protections Against Fraudulent or Abusive Practices.

Expand Disclosures for High LTV Mortgages. Consumers with high credit card debts are frequently offered second mortgages to consolidate their debts, extend the time for repayment, and reduce the interest rate. These mortgages can result in debt levels of 125% to 150% of the home's value. Consumers may not understand the consequences of these refinancings -- especially that the failure to repay these consumer debts could lead to losing their home -- and recent studies show that many such homeowners promptly incur new consumer credit debts. We support legislation requiring lenders on high loan-to-value second mortgages to disclose that: (1) interest payments may not be fully deductible; (2) the consumer may be unable to resell the house unless the loan amount is significantly repaid; and (3) default can result in foreclosure.

Increase Civil Liability Limits for the Truth in Lending Act (TILA) Violations. TILA provides an individual right of action for violations under which a consumer can recover actual damages, additional statutory damages, and court costs. The amount of damages, however, is limited to a range of not less than $100 nor greater than $1,000 for non-mortgage loans or leases, and to a range of $200 to $2000 for mortgage loans. These damage limits may be too low to deter TILA violations, particularly at unregulated institutions not subject to systematic and regular examinations. We support raising the statutory cap to a level sufficient to deter violations.

Improved Reporting on Race, Income and Other Data. Financial institutions are required under the Home Mortgage Disclosure Act (HMDA) to report the race, income and other data about home mortgage borrowers, but a separate Federal Reserve regulation prohibits them from collecting such information for non-mortgage borrowers. Experience suggests that publicizing such data helps to reduce discrimination, increase access for minority borrowers, and foster innovation, and the current prohibition inhibits self-testing under the fair lending laws and makes fair lending enforcement more difficult. The Treasury Department has asked the Federal Reserve to amend the regulation to allow increased reporting.

Clear Reporting. HMDA regulations do not require financial institutions to report separately on sub-prime loans, such as for manufactured housing. If these loans were identified separately, banking regulators and enforcement agencies could better analyze the data for potential fair lending problems. In addition, financial institutions should be required to report on the reasons for loan denials. The Treasury Department has asked the Federal Reserve to determine if these regulatory changes can be made.

Limitations on HMDA. Institutions, other than banks and thrifts, do not have to report under HMDA if fewer than 10% of their loans are made for home purchase. The effect of this rule is to exclude from reporting some of the largest and fastest growing mortgage providers in the country, whose consumer loan portfolio is also large. We are asking the Federal Reserve to bring such providers under HMDA coverage.

Prohibit Coercive Sales of Insurance Products. Borrowers buy credit insurance to ensure repayment of their mortgages in the event of death, injury or job loss. However, the economic value to the consumer of these products is dubious. Moreover, credit insurance is frequently marketed in a way that is either explicitly or implicitly coercive -- that is, consumers are told or left with the impression that their chances of getting the loan or getting it more quickly would improve if they purchased the insurance. Some creditors collect up-front lump-sum insurance premiums for the policy term, so consumers cannot cancel. Required disclosures appear to be ineffective at deterring these practices. We support legislation barring the advance collection of lump-sum insurance premiums, so that consumers can pay for the insurance one month at a time, and so loan termination automatically cancels both coverage and liability for insurance payments. In addition, Congress should bar the solicitation of credit life insurance until the lender has approved the loan application and communicated approval to the borrower.

Limit Consumer Liability for Non-PIN Protected Debit Cards. "Off-line debit cards" allow consumers to pay for products through an electronic transfer at the point of sale. These "check cards" differ from "on-line" ATM cards because there is no PIN or other security feature (other than a signature) to authenticate the transaction. Although credit cards also carry no PIN protection, the consumer is generally only liable for no more than $50 of unauthorized charges. But with debit cards losses can be much higher unless the customer quickly notices and reports the loss. Thus, consumers can get the worst of both worlds: higher exposure to loss without security protections. Consumer liability for these cards should be limited as it is currently limited for credit cards -- a step that VISA and Mastercard have already taken voluntarily.

Prohibit Unsolicited Mailing of Loan Checks. Loan checks are credit products for which the consumer need only sign and cash the check to obtain a loan. Because these unsolicited checks are "live," however, the consumer is also at risk for fraudulent endorsement of the check. For the same reasons that Federal law prohibits unsolicited mailing of credit cards -- protecting consumers from the hassle of contesting liability for stolen card purchases -- we support legislation prohibiting unsolicited mailing of loan checks. Consumers should not feel they have to shred their daily mail.

Reform Accounting Rules for Consumer Installment Loans. We support legislation to eliminate the use of the "rule of 78," an outmoded accounting rule that disadvantages borrowers, for all consumer credit transactions. In 1992, Congress barred the rule's use in loans with terms over 61 months; our proposal would finish the task. Creditors would have to use an accounting method at least as favorable to the consumer as the actuarial method.

Take Action Against "Sub-prime" Lending Abuses.

Expand Protections in the Home Equity Market. The Fed/HUD Report on RESPA and TILA documented continued problems with abusive practices in some segments of the mortgage market, including evasions of the Home Ownership Equity Protection Act (HOEPA), which provides protections for borrowers with high-cost loans. The study recommended targeting abusive practices. For example: to reduce the occurrence of loan flipping -- recurrent refinancings that may make it difficult for a home owner to pay off a loan or to sell her home -- financing fees in high cost loans covered by HOEPA should be regulated; prepayment penalties and balloon payments should be further restricted; and the HOEPA threshold should be lowered. Creditors should be required to provide additional data on HOEPA loans. All amounts paid by a borrower should be counted under the HOEPA trigger. Creditors should be required to inform high-cost-loan applicants of available home counseling programs prior to closing. We will work with Congress to increase protections in this area.

Expand Enforcement Tools Against Abusive Practices. Congress should eliminate the requirement for a showing of "pattern or practice" of asset-based lending to establish HOEPA violations. The definition of "creditor" should be expanded to include individuals that control the lending practices of a company to deal with the problem of small, thinly capitalized sub-prime lenders who escape HOEPA liability by dissolution or bankruptcy. Finally, Congress should strengthen RESPA enforcement and remedies, consistent with the recommendations in the Fed/HUD Report.

Improve HMDA Reporting. There is a current imbalance in reporting requirements and enforcement under HMDA as between regulated depository institutions and other mortgage lenders. Some unregulated lenders do not have to report all their loans, and face no sanctions if they fail to report when required. We support legislation providing HUD with enforcement authority to assure compliance by all lenders with HMDA reporting, unless banking regulators are already enforcing HMDA with respect to such lenders. These legislative changes will help level the playing field on reporting and compliance between regulated and unregulated financial institutions, and will improve disclosure in a growing segment of the mortgage lending market.

The Banking Regulators Should Continue to Improve Guidance on Sub-prime Lending. The Federal Financial Institutions Examination Council is improving guidance on fair lending compliance. The FFIEC issued fair lending examination procedures for banking regulators in January 1999 and focused particular attention on the problem of "steering" loan applicants on a prohibited basis to a sub-prime lender within a financial institution's organization. In March, the FFIEC released additional guidance focused on safety and soundness issues and fair lending problems. The OCC recently issued guidance warning of the risks in this area. Today, the President is directing the Office of the Comptroller of the Currency and the Office of Thrift Supervision, in consultation with HUD, the FTC, the Justice Department, and the other banking regulators, to study whether further actions are necessary to halt abusive practices in the sub-prime area.

EXPAND ACCESS TO FINANCIAL SERVICES

Provide Low-Cost Banking Services to All Americans. Too many Americans cannot afford, or do not have access to, basic banking services. The Administration will increase and strengthen its efforts -- working with banks and consumer groups -- to increase access to low-cost banking services to all Americans. As part of this effort, Treasury is finalizing a program to pay set-up costs for low-fee basic banking accounts for federal benefit recipients.

Provide Individual Development Accounts (IDAs) To Make It Easier for Low-Income Families to Save. IDAs allow low-income households to save not just for retirement but also for education, emergencies, home ownership, or business investment. Individual contributions can be matched to encourage more savings. (The FY 2000 budget doubles funding for IDAs.)

Bolster the Community Development Financial Institutions (CDFI) Fund. Treasury's CDFI Fund provides grants, loans, and equity investments to locally-based, specialized financial institutions and mainstream banks and thrifts serving low and moderate income communities. The CDFI Fund is helping to expand the reach of these institutions to under served communities. The Administration is seeking $125 million for the Fund in FY 2000 and Fund reauthorization.

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IMPROVE CONSUMER FINANCIAL EDUCATION

Launch a Campaign to Promote Education on Credit, Savings, and Investment. One of the best protections for consumers is education. Yet evidence suggests that consumers often find credit and investment opportunities confusing, and are carrying greater levels of debt, filing bankruptcy more often, not saving as much as they would like for retirement, and investing without full comprehension of the risks involved. The President today directed his National Economic Council to convene a high level interagency task force to present him with a plan to raise financial literacy levels, and to expand the Administration's commitment to public and private consumer financial education programs. Elements of this plan will include:

Identify and Publicize Successful 'Best Practices" for High School and Other Financial Education Programs. Nonprofit groups, such as the National Council on Economic Education and JumpStart, as well as government agencies including the Department of Agriculture and the Department of Defense, have developed educational modules and course materials that not only improve students' understanding of complex financial topics but also have been shown to improve their long-term financial status. Working with the interagency task force, the Department of Education will help publicize proven educational programs, to make it easier for teachers, professors, and other educators to adopt financial education programs that work.

Promote Effective Financial Planning. Studies show that families who are able to develop and follow a financial plan are much more successful in achieving major financial goals, such as saving adequately for retirement, their children's education, or a new business venture. A growing number of public, nonprofit, and corporate initiatives have begun to educate Americans about effective financial planning, such as the campaigns sponsored by the American Savings Education Council, the Securities and Exchange Commission, and the Department of Labor. The Administration will participate in joint initiatives with these and other groups to highlight the benefits of personal financial planning and the steps that all Americans can take to make financial planning easier.

THE CLINTON-GORE PLAN FOR FINANCIAL PRIVACY AND CONSUMER PROTECTION IN THE 21st CENTURY

May 04, 1999

DETAILED PROPOSAL SUMMARY

INTRODUCTION

Technology and competition in financial services give Americans more complex choices than ever before. Innovations in the financial marketplace offer millions of consumers new, ever increasing choices for investing their savings and obtaining credit. But new products have brought new risks and new abusive practices. We must update our consumer protection laws to give consumers the power, information and protection they need to profit from our 21st Century financial system.

Members of Congress, including Ranking Members Sarbanes and LaFalce, have sponsored important legislation to modernize our consumer financial protection laws. We applaud their leadership and look forward to working with Congress on a consumer protection agenda.

Set forth below is a series of actions that the Clinton Administration believes should be part of this agenda. The list is not exhaustive, and we will continue to look for constructive ideas in these and other areas. Among the issues deserving further scrutiny are lending practices such as "pay day" loans (short-term loans which can carry interest rates of 400%) and bank check processing practices that may be designed to maximize bounced check fees. We will work with the states and the FTC wherever possible. Secretary Cuomo is making important efforts to address abusive mortgage lending practices.

PROTECT FINANCIAL PRIVACY

Require institutions to inform consumers of plans to share or sell their financial information, and give the consumer the power to stop it. Although consumers put great value on the privacy of their financial records, our laws have not caught up to technological developments that make it possible and potentially profitable for companies to share financial data in new ways. Current law does provide some privacy protections: for example, the Fair Credit Reporting Act (FCRA) requires a form of notice and opt-out before certain information about consumers (e.g., information provided on an account application) can be shared. But there are no limits on the sharing of information about consumers' transactions (e.g., account balances, who they write checks to) within a financial conglomerate, or even on the sale of that information to a third party. We support legislation to give consumers control over the use and sharing of <u>all</u> their financial information.

Impose special restrictions on any sharing of medical information within a financial conglomerate. One of our greatest privacy concerns involve medical information. Yet, cross-industry mergers and consolidation have given banks unprecedented access to consumers' medical records. We support legislation requiring that medical information, such as that gathered from life insurance records, not be shared within financial services conglomerates (e.g., between banking and insurance affiliates) or with third parties, except for narrowly defined purposes. Consumers who undergo physical exams to obtain insurance, for example, should not have to fear that the information will be used to lower their credit card limits or deny them mortgages.

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Combat Internet Securities Risk and Fraud with Investor Education and Enforcement. More and more Americans are investing in the stock market; 5.6 million are now trading on-line. The technology opens up great opportunity, but the rewards are not without risks. Complaints to the SEC were up 330% in one year, and new securities fraud schemes are uncovered each day. SEC Chairman Levitt is launching a stepped-up SEC effort to arm investors with the information they need to understand and manage the risks and protect themselves against fraud. In addition, President Clinton's budget provided $11 million in new funds for SEC enforcement; however, the rate of growth in Internet trading and abuse has exceeded expectations. To meet this need, President Clinton will work with Congress and Chairman Levitt to provide an additional $5.5 million for SEC enforcement, beyond what was requested in the FY 2000 balanced budget. These funds will help the SEC better investigate and prosecute Internet securities fraud. It will specifically help the Commission increase Internet surveillance, enhance the SEC's Enforcement

Complaint Center, augment training for law enforcement on how to recognize and prosecute Internet securities fraud and continue its efforts to educate investors about the risk and rewards of investing over the Internet.

Internet Fraud Initiative: Federal, state and local law enforcement officials and regulatory agencies are receiving a growing number of complaints from consumers about Internet fraud. Many of the same features of the Internet that make it a powerful tool for legitimate e-commerce (global reach, instant and often anonymous communications, ability to reach millions of consumers) -- also make it attractive for fraud schemes. The Internet Fraud Initiative will crack down on Internet fraud by, for example, stepping up training for federal, state, and local prosecutors and agents; developing information on the nature and scope of Internet fraud; and keeping the public better informed about current fraud schemes and how to handle them. The initiative will also help coordinate the efforts of federal (Department of Justice, the FBI, the U.S. Secret Service, the Postal Inspection Service, the Federal Trade Commission, and the Securities and Exchange Commission), state and local law enforcement agencies.

Criminalize "Pretext Calling." There are widespread reports of private investigators and data brokers tricking financial institutions into providing confidential customer information. We support legislation that would criminalize this practice and protect the privacy and security of consumer financial information.

Fully Implement FTC-HELP and Consumer Sentinel. The Year 2000 will be the first full year of operation for FTC's toll-free consumer hotline, part of the Commission's Consumer Response Center. The hotline will give consumers fast and easy access to information they need to protect themselves -- from tips about credit and debt collection to advice on how to avoid becoming a victim of fraud. Complaints to the hotline become part of the Consumer Sentinel, the FTC's fraud database, which is shared only with other law enforcers in the U.S. and Canada. By 2000, the Consumer Sentinel database is expected to be a primary tool in the fight against consumer fraud. The President's FY2000 budget funds Consumer Sentinel.

Improve Consumer Protections Against Fraudulent or Abusive Practices.

Expand Disclosures for High LTV Mortgages. Consumers with high credit card debts are frequently offered second mortgages to consolidate their debts, extend the time for repayment, and reduce the interest rate. These mortgages can result in debt levels of 125% to 150% of the home's value. Consumers may not understand the consequences of these refinancings -- especially that the failure to repay these consumer debts could lead to losing their home -- and recent studies show that many such homeowners promptly incur new consumer credit debts. We support legislation requiring lenders on high loan-to-value second mortgages to disclose that: (1) interest payments may not be fully deductible; (2) the consumer may be unable to resell the house unless the loan amount is significantly repaid; and (3) default can result in foreclosure.

Increase Civil Liability Limits for the Truth in Lending Act (TILA) Violations. TILA provides an individual right of action for violations under which a consumer can recover actual damages, additional statutory damages, and court costs. The amount of damages, however, is limited to a range of not less than $100 nor greater than $1,000 for non-mortgage loans or leases, and to a range of $200 to $2000 for mortgage loans. These damage limits may be too low to deter TILA violations, particularly at unregulated institutions not subject to systematic and regular examinations. We support raising the statutory cap to a level sufficient to deter violations.

Improved Reporting on Race, Income and Other Data. Financial institutions are required under the Home Mortgage Disclosure Act (HMDA) to report the race, income and other data about home mortgage borrowers, but a separate Federal Reserve regulation prohibits them from collecting such information for non-mortgage borrowers. Experience suggests that publicizing such data helps to reduce discrimination, increase access for minority borrowers, and foster innovation, and the current prohibition inhibits self-testing under the fair lending laws and makes fair lending enforcement more difficult. The Treasury Department has asked the Federal Reserve to amend the regulation to allow increased reporting.

Clear Reporting. HMDA regulations do not require financial institutions to report separately on sub-prime loans, such as for manufactured housing. If these loans were identified separately, banking regulators and enforcement agencies could better analyze the data for potential fair lending problems. In addition, financial institutions should be required to report on the reasons for loan denials. The Treasury Department has asked the Federal Reserve to determine if these regulatory changes can be made.

Limitations on HMDA. Institutions, other than banks and thrifts, do not have to report under HMDA if fewer than 10% of their loans are made for home purchase. The effect of this rule is to exclude from reporting some of the largest and fastest growing mortgage providers in the country, whose consumer loan portfolio is also large. We are asking the Federal Reserve to bring such providers under HMDA coverage.

End Coercive Sales of Insurance Products. Borrowers buy credit insurance to ensure repayment of their mortgages in the event of death, injury or job loss. However, the economic value to the consumer of these products is dubious. Moreover, credit insurance is frequently marketed in a way that is either explicitly or implicitly coercive -- that is, consumers are told or left with the impression that their chances of getting the loan or getting it more quickly would improve if they purchased the insurance. Some creditors collect up-front lump-sum insurance premiums for the policy term, so consumers cannot cancel. Required disclosures appear to be ineffective at deterring these practices. We support legislation barring the advance collection of lump-sum insurance premiums, so that consumers can pay for the insurance one month at a time, and so loan termination automatically cancels both coverage and liability for insurance payments. In addition, Congress should bar the solicitation of credit life insurance until the lender has approved the loan application and communicated approval to the borrower.

Limit Consumer Liability for Non-PIN Protected Debit Cards. "Off-line debit cards" allow consumers to pay for products through an electronic transfer at the point of sale. These "check cards" differ from "on-line" ATM cards because there is no PIN or other security feature (other than a signature) to authenticate the transaction. Although credit cards also carry no PIN protection, the consumer is generally only liable for no more than $50 of unauthorized charges. But with debit cards losses can be much higher unless the customer quickly notices and reports the loss. Thus, consumers can get the worst of both worlds: higher exposure to loss without security protections. Consumer liability for these cards should be limited as it is currently limited for credit cards -- a step that VISA and Mastercard have already taken voluntarily.

Prohibit Unsolicited Mailing of Loan Checks. Loan checks are credit products for which the consumer need only sign and cash the check to obtain a loan. Because these unsolicited checks are "live," however, the consumer is also at risk for fraudulent endorsement of the check. For the same reasons that Federal law prohibits unsolicited mailing of credit cards -- protecting consumers from the hassle of contesting liability for stolen card purchases -- we support legislation prohibiting unsolicited mailing of loan checks. Consumers should not feel they have to shred their daily mail.

Reform Accounting Rules for Consumer Installment Loans. We support legislation to eliminate the use of the "rule of 78," an outmoded accounting rule that disadvantages borrowers, for all consumer credit transactions. In 1992, Congress barred the rule's use in loans with terms over 61 months; our proposal would finish the task. Creditors would have to use an accounting method at least as favorable to the consumer as the actuarial method.

Take Action Against "Sub-prime" Lending Abuses.

Expand Protections in the Home Equity Market. The Fed/HUD Report on RESPA and TILA documented continued problems with abusive practices in some segments of the mortgage market, including evasions of the Home Ownership Equity Protection Act (HOEPA), which provides protections for borrowers with high-cost loans. The study recommended targeting abusive practices. For example: to reduce the occurrence of loan flipping -- recurrent refinancings that may make it difficult for a home owner to pay off a loan or to sell her home -- financing fees in high cost loans covered by HOEPA should be regulated; prepayment penalties and balloon payments should be further restricted; and the HOEPA threshold should be lowered. Creditors should be required to provide additional data on HOEPA loans. All amounts paid by a borrower should be counted under the HOEPA trigger. Creditors should be required to inform high-cost-loan applicants of available home counseling programs prior to closing. We will work with Congress to increase protections in this area.

Expand Enforcement Tools Against Abusive Practices. Congress should eliminate the requirement for a showing of "pattern or practice" of asset-based lending to establish HOEPA violations. The definition of "creditor" should be expanded to include individuals that control the lending practices of a company to deal with the problem of small, thinly capitalized sub-prime lenders who escape HOEPA liability by dissolution or bankruptcy. Finally, Congress should strengthen RESPA enforcement and remedies, consistent with the recommendations in the Fed/HUD Report.

Improve HMDA Reporting. There is a current imbalance in reporting requirements and enforcement under HMDA as between regulated depository institutions and other mortgage lenders. Some unregulated lenders face no sanctions if they fail to report when required. We support legislation providing HUD with enforcement authority to assure compliance by all lenders with HMDA reporting, unless banking regulators are already enforcing HMDA with respect to such lenders. These legislative changes will help level the playing field on reporting and compliance between regulated and unregulated financial institutions, and will improve disclosure in a growing segment of the mortgage lending market.

The Banking Regulators Should Continue to Improve Guidance on Sub-prime Lending. The Federal Financial Institutions Examination Council is improving guidance on fair lending compliance. The FFIEC issued fair lending examination procedures for banking regulators in January 1999 and focused particular attention on the problem of "steering" loan applicants on a prohibited basis to a sub-prime lender within a financial institution's organization. In March, the FFIEC released additional guidance focused on safety and soundness issues and fair lending problems. The OCC recently issued guidance warning of the risks in this area. Today, the President is directing the Office of the Comptroller of the Currency and the Office of Thrift Supervision, in consultation with HUD, the FTC, the Justice Department, and the other banking regulators, to study whether further actions are necessary to halt abusive practices in the sub-prime area.

EXPAND ACCESS TO FINANCIAL SERVICES

Provide Low-Cost Banking Services to All Americans. Too many Americans cannot afford, or do not have access to, basic banking services. The Administration will increase and strengthen its efforts -- working with banks and consumer groups -- to increase access to low-cost banking services to all Americans. The Treasury Department will pay set-up costs to encourage private banks to offer low-fee banking accounts for those who receive federal benefits like Social Security.

Provide Individual Development Accounts (IDAs) To Make It Easier for Low-Income Families to Save. IDAs allow low-income households to save not just for retirement but also for education, emergencies, home ownership, or business investment. Individual contributions can be matched to encourage more savings. (The FY 2000 budget doubles funding for IDAs.)

Bolster the Community Development Financial Institutions (CDFI) Fund. Treasury's CDFI Fund provides grants, loans, and equity investments to locally-based, specialized financial institutions and mainstream banks and thrifts serving low and moderate income communities.

The CDFI Fund is helping to expand the reach of these institutions to under served communities. The Administration is seeking $125 million for the Fund in FY 2000 and Fund reauthorization.

IMPROVE CONSUMER FINANCIAL EDUCATION

Launch a Campaign to Promote Education on Credit, Savings, and Investment. One of the best protections for consumers is education. Yet evidence suggests that consumers often find credit and investment opportunities confusing, and are carrying greater levels of debt, filing bankruptcy more often, not saving as much as they would like for retirement, and investing without full comprehension of the risks involved. The President today directed his National Economic Council to convene a high level interagency task force to present him with a plan to raise financial literacy levels, and to expand the Administration's commitment to public and private consumer financial education programs. Elements of this plan will include:

Identify and Publicize Successful 'Best Practices" for High School and Other Financial Education Programs. Nonprofit groups, such as the National Council on Economic Education and JumpStart, as well as government agencies including the Department of Agriculture and the Department of Defense, have developed educational modules and course materials that not only improve students' understanding of complex financial topics but also have been shown to improve their long-term financial status. Working with the interagency task force, the Department of Education will help publicize proven educational programs, to make it easier for teachers, professors, and other educators to adopt financial education programs that work.

Promote Effective Financial Planning. Studies show that families who are able to develop and follow a financial plan are much more successful in achieving major financial goals, such as saving adequately for retirement, their children's education, or a new business venture. A growing number of public, nonprofit, and corporate initiatives have begun to educate Americans about effective financial planning, such as the campaigns sponsored by the American Savings Education Council, the Securities and Exchange Commission, and the Department of Labor. The Administration will participate in joint initiatives with these and other groups to highlight the benefits of personal financial planning and the steps that all Americans can take to make financial planning easier.

Consumer Finance

THE CLINTON-GORE PLAN FOR FINANCIAL PRIVACY AND CONSUMER PROTECTION IN THE 21st CENTURY

May 4, 1999

Today, President Clinton Introduces Legislative Proposals and Executive Action to Protect Consumers in the New Economy, Based on Five Principles: (1) Protect Financial Privacy; (2) Expand the Consumer's Right to Know; (3) Prevent Fraud and Abusive Practices; (4) Expand Access to Financial services; (5) Educate Consumers.

PROTECT FINANCIAL PRIVACY. Cross-industry mergers and consolidation have given banks unprecedented access to consumers' financial and medical records at just the time when new technologies have made it possible -- and potentially profitable -- for banks to mine such data. President Clinton believes that consumers deserve notice and choice about the use of their personal information, and Vice President Gore has led the Administration's efforts to protect consumers' financial and medical privacy in the new financial marketplace. Today, President Clinton will call on Congress to:

✓ **Give Consumers More Power Over Their Own Information.** Require institutions to inform consumers of plans to share or sell their financial information; give the consumer the power to stop it. Current law does not limit on selling or sharing of information about consumers' transactions.

✓ **Protect Medical Information.** Impose special restrictions on any sharing of medical information within a financial conglomerate. As banks and insurance firms merge, for example, consumers should not fear that that the results of a physical exam could be used to make a credit decision.

EXPAND THE CONSUMER'S RIGHT TO KNOW. Consumers face a bewildering array of choices in today's financial marketplace and often do not have sufficient information to make wise decisions. Aggressive marketing can obscure the truth about the financial choices a customer is being asked to make. For example, consumers are often surprised when low introductory credit card rates expire and interest rates spike. To address this, President Clinton will urge Congress to:

✓ **Improve Credit Card Disclosures.** Prevent misleading marketing of "teaser rates" by requiring equally prominent disclosure of expiration dates of low rates, eventual terms, and possible penalties; require disclosure of how long and how costly repayment would be if a consumer makes only the minimum payment.

✓ **Improve Disclosure Rules.** Improve disclosure rules for Internet credit card solicitations.

✓ **Require Greater Disclosure for Other Financial Products.** To allow consumers to comparison shop, require enhanced disclosures for rent-to-own arrangements, home mortgages and settlement services, and international money transfers.

✓ **Require Dual ATM Disclosures.** Require ATMs to provide disclosure of surcharges on the machine and the terminal screen, so consumers can shop with their feet.

PREVENT FRAUD AND ABUSIVE PRACTICES. More and more Americans are using the Internet to invest in the stock market and conduct other financial transactions. Fraud schemes -- including stock manipulation -- are uncovered each day. Off-line, old fraudulent practices continue, and new ones -- such as identity theft and on-line schemes -- continue to arise. Low-income borrowers must often turn to unregulated, high-cost lenders whose terms are sometimes abusive. To crack down on financial fraud and attack other abuses, the Clinton Administration will:

- ✓ **Seek Increased Funding for SEC Efforts.** Work with Congress to provide to the SEC $16.5 million ($5.5 million in addition to the $11 million increase in the FY00 budget) to increase Internet prosecutions and surveillance, enhance the SEC's Enforcement Complaint Center, and augment training for law enforcement on Internet securities fraud.

- ✓ **Fight Identity Theft.** Launch a vigorous identity theft enforcement and prevention strategy led by the Treasury Department.

- ✓ **Fight Internet Fraud.** Crack down on Internet fraud under an effort led by the Department of Justice that will step up law enforcement training and public education.

- ✓ **Stop Sub-prime Lending Abuse.** Improve reporting of high-cost mortgage loans and give the FTC and HUD adequate authority to stop sub-prime lending abuses.

EXPAND ACCESS TO FINANCIAL SERVICES. Too many Americans cannot afford, or do not have access to, basic banking services. The Administration will strengthen its efforts -- working with banks and consumer groups -- to expand access to low-cost banking services to all Americans.

- ✓ **Low-Fee Banking Accounts for Federal Beneficiaries.** The Treasury Department will pay set-up costs to encourage private banks to offer low-fee banking accounts for those who receive federal benefits like Social Security.

- ✓ **Expand Individual Development Accounts (IDAs).** The President's balanced budget would provide additional funds for accounts that allow low-income families to save for education, emergencies, homeownership or business.

- ✓ **Bolster the Community Development Financial Institutions (CDFI) Fund.** The President's balanced budget would increase funding for grants, loans, and equity investments in local institutions serving low and moderate income communities.

EDUCATE CONSUMERS AND IMPROVE FINANCIAL LITERACY. The daunting complexity of financial products and choices increases the importance of consumer financial education.

✓ **A Plan to Raise Financial Literacy**. President Clinton today directed that the National Economic Council to prepare an interagency plan to raise financial literacy and increase the government's support for consumer financial education. Under the plan, for example, the Department of Education will publicize proven educational programs that integrate financial literacy into basic school curricula.

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