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Date: Sept. 29, 2004

DOCUMENT NO. & TYPE	SUBJECT/TITLE	DATE	RESTRICTION
1. List	re: Consumer Financial Services Working Group, 1p. (partial)	n.d.	P6/B6

RESTRICTIONS

P1 National security classified information [(a)(1) of the PRA].
P2 Relating to appointment to Federal office [(a)(2) of the PRA].
P3 Release would violate a Federal statute [(a)(3) of the PRA].
P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA].
P5 Release would disclose confidential advice between the President and his advisors, or between such advisors [(a)(5) of the PRA].
P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA].

PRM Personal records misfile defined in accordance with 44 USC 2201 (3).

B1 National security classified information [(b) (1) of the FOIA].
B2 Release could disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA].
B3 Release would violate a Federal statute [(b)(3) of the FOIA].
B4 Release would disclose trade secrets or confidential commercial financial information [(b)(4) of the FOIA].
B6 Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA].
B7 Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA].
B8 Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA].
B9 Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA].

June 15, 1999

MEMORANDUM TO JOHN PODESTA

FROM: SARAH ROSEN, NEC

RE: JUNE 16TH FINANCIAL MODERNIZATION CONFERENCE CALL

Attached please find an excellent memorandum from Treasury prepared for you as background for this call. As the memorandum notes, the Administration's primary objective for the call is to make clear that Secretary Rubin's departure will not occasion a change in Administration position on CRA and choice in operating structure. However, **privacy** may be the topic foremost on the minds of the CEOs on the call.

Gene Sperling and Gary Gensler hosted a meeting of industry trade groups on Monday to discuss Financial Modernization. If that meeting is any guide, virtually every question you get will be about privacy. For that reason, I provide further background on this issue.

The President's Proposals

On May 4, 1999, President Clinton announced a five-prong strategy for "Financial Privacy and Consumer Protection in the 21st Century." The first prong was privacy, including three legislative proposals.

- **Notice and Opt-Out Before Sharing with Affiliates or Third Parties.** 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 all their financial information.

- **Limit Sharing of Medical Information within a Financial Conglomerate.** One of Americans' greatest privacy concerns involves 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.

- **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.

Current Legislative Status of Privacy

Over the last few months, momentum on privacy has built. The Senate bill contained a ban on pretext calling but no new privacy protections. While Senate Democrats, including Senator Sarbanes, are avid proponents of privacy, they agreed that further progress on the issue could be addressed separately. The Senate Banking Committee is holding a series of hearings on the issue this month.

The House Banking Committee reached bipartisan consensus on modest provisions -- a ban on sharing medical information within financial conglomerates (with imperfect language) and a requirement of notice (but no choice) before sharing transactional information.

In the House Commerce Committee, Democrats led by Representative Markey were not willing to compromise. In a surprising turn of events, Republicans agreed to an amendment during mark-up that was effectively two of the President's proposals: (1) it requires notice and opt-out before transactional information can be shared with third parties or affiliates; and (2) it bans sharing medical information within financial conglomerates.

Two events last week propelled the Republicans to reverse their prior course of deflecting privacy proposals: (1) Acting Comptroller Hawke called bank privacy practices "seamy"; and (2) the Minnesota Attorney General filed a suit against U.S. Bancorp alleging that its bank had sold personal account information to telemarketers for a cut of the profits. The latter event especially infuriated members, as bank lobbyists had been telling them that banks did not sell information to third parties – only wanted to protect it for use by affiliates.

Administration Concerns With Commerce Committee Language

The Administration does have a few concerns with the Commerce Committee's privacy language:

- **Enforcement Authority:** The bill does not expand – as we recommended – bank regulator ability to examine for compliance with privacy requirements; and it gives all rulemaking and enforcement authority for the bill to the FTC – not to the bank and securities regulators.

- **Coverage of Non-Regulated Financial Institutions:** The bill covers only bank holding companies – not non-bank financial institutions like finance or mortgage companies. Fairness to regulated entities and consumer protection would recommend expanding coverage.

- **Need For Possible Exceptions:** There may be unintended consequences of the proposal if, for example, it creates barriers to fraud detection or processing efficiency. We would be willing to work with industry to better understand what exceptions, if any, are necessary.

Administration Strategy on Privacy and Financial Modernization

It is too early to tell whether there will be any conflict between two Administration goals. Treasury is implementing a carefully laid strategy to win support for the President's position on CRA and operating structure choice. The privacy issue adds a new – and as yet unpredictable – variable. If possible, we also want to achieve a victory for the President and consumers by seeing Congress adopt the President's privacy proposals.

Talking Points

During the Sperling/Gensler meeting with industry representatives, they pleaded for Administration support for consideration of privacy outside the context of Financial Modernization. Gene gave them no encouragement that we would help them stall on privacy, nor did he say that we would insist on its inclusion; however, he was very effective making the following points in response:

- **The President has clearly stated his policy objectives in the area of privacy.**

- **The momentum on this issue is going only one way; Congress seems increasingly likely to address this issue quickly given its deep-rooted populist appeal.**

- **You can resist that momentum or you can try to work with us to determine how your legitimate "technical" concerns can be accomplished consistent with the President's stated policy objectives.**

- **That work will be time well spent, regardless of the vehicle Congress chooses to address privacy. The issue is not going to go away.**

Attachment

BACKGROUND ON CRA ISSUES IN FINANCIAL MODERNIZATION
September 20, 1999

On August 6, 1999, a letter signed by over sixty organizations was sent to the President. (See attached.) The letter expressed the groups' appreciation for the President's "consistent support of the ... [CRA] throughout the consideration of financial deregulation legislation." It also adds:

> "[Y]our forceful support is needed now more than ever.... The conference holds special dangers for CRA and the future of urban and rural communities."

> "As you have pointed out, the Senate bill rolls back CRA. The Senate version is pitted against a House bill, which essentially contains a bare bones, status quo approach to CRA. This leaves no room for traditional compromises where House and Senate conferees simply "split the differences." While there are many provisions in the legislation where splitting the difference might work well, it would be a disaster for CRA, and would negate your efforts to preserve and reinvigorate the Act."

Finally, the letter asks the President to let the Congress know that he will not sign any bill that contains any of the three provisions that undermine CRA or fails to contain the two provisions that preserve CRA. (For your reference, the five issues mentioned in the letter, the position of the advocacy groups, and the Administration's views on these issues are all detailed below.)

The Leadership Conference for Civil Rights is not a signatory to the letter; however, a few of the groups attending your meeting are signatories and the letter reflects the full inventory of CRA-related concerns of low-income advocates.

Note that Treasury has been asked to draft a reply to the groups' letter to the President on CRA. (The draft was delayed because Cliff Kellogg just had a baby, but they promise a draft this week.) It will present an opportunity for us to be a bit more specific on the nature of our veto threat than we have been before, without eliminating all flexibility for a compromise that saves face for Gramm.

Senator Gramm – Signaling Interest in a Compromise on CRA

In a September 15th meeting between the leading players in the Fin Mod conference (Gramm, Sarbanes, Leach, LaFalce, and Bliley – Dingell was unavailable), Senator Gramm's posture was reportedly constructive. On CRA, he indicated that he wanted three things: (1) the sunshine amendment; (2) limitations on penalties for have and maintain; and (3) eliminate reporting requirements and enforcement mechanisms for small banks (not a full small bank exemption as previously proposed, but effectively similar). In public statements, Gramm has focused on the importance of the first two items. Conventional wisdom says that, in these two areas, some compromise (face-saving for Gramm) will be possible. (These issues are explained in more detail below.)

Small Bank Exemption

> *Description:* The Senate bill would exempt from CRA rural institutions under $100 million. This would exempt 72% of non-metropolitan banks (3893) from community responsibility. No comparable House provision.

Groups' View: "It is not the size of the bank that counts; it is the size of the needs of the citizens that live in the communities whose convenience and needs these banks are chartered to serve."

Administration Position: In 1995, the Administration threatened to veto the Financial Institutions Regulatory Relief bill in significant part because it contained a (much larger) small bank exemption from CRA. Although we have not specifically itemized CRA provisions that we would veto, we have said that the President would not sign a bill that weakened CRA. It is widely assumed inside the Administration and on the Hill, that we would veto any small bank exemption from CRA.

Gramm signals: Senator Gramm recently suggested that he just wanted to exempt these institutions from CRA reporting and annual audit requirements. Thus, CRA would apply but there would be no enforcement.

CRA Safe Harbor

Description: The Senate bill provides that banks rated "satisfactory" in the most recent exam and for the last 3 years shall be deemed to be in compliance until their next exam (and thus when a merger or new activities application is filed), unless substantial verifiable information arising since the last exam demonstrating noncompliance is filed with the regulator. The regulator must determine if there is sufficient proof that the bank is no longer in compliance, with the burden on the complainant to show noncompliance. As thousand of institutions are examined for CRA compliance every 24 to 36 months, community groups simply do not have the resources to evaluate CRA performance of each institution on an ongoing basis. They focus their attention on institutions that have applied for merger or branch approval. This would dramatically diminish their ability to raise questions about community service at the time when that question is most relevant. There is no comparable provision in the House bill.

Groups' View: "The bill places a gag on citizens and communities, effectively blocking meaningful public comment on banks' lending performance when they seek to merge or otherwise expand."

Administration Position: While we have not itemized which CRA provisions would prompt a veto, we have said we would veto if the bill weakened CRA. It is assumed that this provision is entirely unacceptable.

Gramm Signals: Gramm has not mentioned this provision in recent comments on CRA.

Sunshine Amendment

Description: Senate bill requires that any "CRA agreement" be filed with regulator and disclosed to public. Also requires reporting to regulators about activities under the agreement. If not disclosed, agreement is unenforceable. "CRA agreements" are any between bank and non-governmental entity with a value of $10k or more. No comparable House provision.

Groups' View: The bill "also contains an unacceptable amendment (under the guise of "sunshine") which will create mounds of meaningless paperwork and discourage the cooperation and agreements which your administration has attempted to foster between banks and community groups as part of mutually beneficial community development efforts." Despite this statement, we believe that some groups are more open to some sunshine provisions remaining than others.

Administration Position: While grossly over-broad (might be read to cover, for example, contracts between banks and mortgage brokers or mortgage insurers involving community lending), the amendment was accepted on the Senate floor by UC. The Administration shared our concerns about its breadth and potential chilling effect privately with both Gramm and Senate Democrats, but we have not made any public statement about the amendment. It is generally thought that the Democrats and Administration cannot be positioned to be against "sunshine." We must not imply that there is something to Senator Gramm's extortion arguments that we are seeking to hide by hiding the terms of these agreements. However, the burden and overbreadth of the amendment should be addressed.

Gramm Signals: Conventional wisdom is that Gramm needs something on "sunshine" as minimal face-saving if he is to compromise on the small bank and safe harbor provisions.

"Have and Maintain" Requirement

Description: The House bill provides that a financial holding company can engage in activities "financial in nature or incidental to..." (i.e., insurance and securities) provided the depository subsidiaries are well capitalized, well managed and "have and maintain" at least a satisfactory CRA rating. Also provides for substantial fines for officers and directors of non-compliant institutions.

Groups' Views: "The House bill does not expand CRA. Rather, it adapts CRA to the changes in bank structure that are authorized by the legislation. It requires that when banks expand through financial holding companies, they have and maintain a satisfactory CRA rating. CRA has always required that the banking regulators consider community lending records when banks expand, and certainly the formation of financial holding companies combining banks with insurance companies and securities firms is a significant expansion."

Administration Position: While never stated in writing, Secretary Rubin told Senate Democrats that the Administration is prepared to veto the bill if "have and maintain" language is not included. We have made clear in various statements that we believe that the absence of "have and maintain" requirement would "weaken CRA." However, we have not gotten involved in the Hill discussions of what penalties and enforcement mechanisms are necessary to ensure that the "have and maintain" requirement is meaningful. As the options have not been fully presented, there may not be a consensus in the Administration yet on what penalty provisions would be acceptable. Democrats on the conference committee also have indicated openness to discuss the penalty provisions for this requirement.

Gramm Signals: Along with sunshine, the penalty issue is one that Gramm recently identified he must have on CRA. He said his simply couldn't allow banks to be incurring million dollar a day penalties for CRA noncompliance. This is his "bottom line."

Wholesale Financial Institutions

Description: The House bill authorizes the establishment of WFIs ("woofies") – uninsured banks that may not receive deposits of less than $100,000. These banks for banks must be well capitalized, well managed, and **are subject to CRA.** The Senate bill does not authorize the establishment of WFIs, so the issue of application of CRA to WFIs did not arise in that bill.

Groups' Views: "The House bill also creates a new class of banks … and simply applies CRA to those banks as it does to other banks. Matching CRA to the changes in bank structure, as dictated by the Congress, is not expansion."

Administration Views: When the Administration proposed its own legislation in 1997, WFIs were subject to CRA. We believe that, if they are created, they should be subject to CRA. However, recently, industry interest in the authority to establish WFIs has dramatically diminished. Thus, the Senate bill has no WFIs at all. It may be easier to simply drop the WFI provisions of the House bill than to have a fight about CRA application, which Gramm claims is CRA expansion.

Gramm Signals: WFIs are not even in the Senate bill.

The Financial Services Act of 1999 - CRA

The Chairmen's mark would seriously weaken CRA and undermine the significant progress that has been made in revitalizing American communities.

* **Failure to Require Maintenance of a Satisfactory CRA Record.** The mark would create a new framework for conducting financial services in the United States but would substantially diminish the role of CRA in this new system. If CRA's relevance is to be preserved when bank and thrift merger activity may become relatively less important compared to the conduct of newly authorized financial activities, banks must have and maintain an adequate record on CRA as a condition for engaging in such activities. In exchange for authority to enter new lines of businesses, the bill should require ongoing compliance with satisfactory CRA performance.

    * The mark contains no requirement that a bank and its depository affiliates have or maintain a satisfactory CRA rating in order for that bank to own a financial subsidiary.
    * The mark contains no enforcement mechanism with regard to CRA and newly authorized financial activities. There is no enforcement of even the minimal "have" requirement because holding companies are not required to file an application for new activities. Regulators should have the authority and discretion to impose reasonable and graduated corrective steps.
    * The mark contains no requirement that the depository institution subsidiaries of a financial holding company have a satisfactory rating at the time the holding company actually engages in expanded activities, since the CRA ratings of banks will only be considered at the time the bank holding company elects to become a financial holding company, and it may be years before it engages in new activities.

* **Small Bank Exemption.** The mark exempts banks with less than $250 million in assets located anywhere, and banks of any size located outside metropolitan areas from timely CRA examinations. This provision would exempt more than 80 percent of banks and thrifts with over 10 percent of assets from timely exams under CRA.

    * This provision exempts more than twice as many banks and thrifts holding more than three times as many assets as under the prior small bank exemption of S. 900. Exams become "stale," requiring updated information within a reasonable time, yet this provision would prohibit examinations more often than once every five years.
    * Since CRA exams for these banks and thrifts are now conducted at the same time as compliance exams, this provision will simply result in confusion and additional exams, not burden relief. These institutions will still be subject to regularly scheduled compliance exams even if their CRA exams happen at a different time.

* **Disclosure and Reporting of Contracts.** The mark requires disclosure of agreements between banks and any private party made pursuant to or in connection with CRA, and reporting on performance under these agreements.

    * While disclosure could be useful, the provision is so broadly worded that it would sweep in a wide range of private contracts that have little or nothing to do with public comment on the application process, and could burden a bank's ability to contract with mortgage brokers and other banks, or to purchase loans or loan pools.
    * Information regarding the dollar amounts, types, locations, and borrower characteristics of loans is already reported by banks subject to CRA.
    * The provision would dramatically increase the paperwork burden under CRA.
    * The provision requires non-bank parties to report on these agreements, despite the fact that banking regulators have no jurisdiction over the general public, and despite the fact that such reporting would duplicate the bank's requirement. This paperwork burden could have a chilling effect on the legitimate lending, service, and investment activities of financial institutions that use community organizations as conduits.

* **CRA Study Designed to be Biased.** The mark requires a study to be conducted that must focus on default rates, delinquency rates, and profitability of loans made under CRA. There is no requirement for the study to evaluate the extent to which CRA has helped to revitalize communities across the United States. Nor is there any requirement that an evaluation be made of the benefits to financial institutions from their charters, including deposit insurance, access to the discount window, or the payments system.

The Financial Services Act of 1999 - Consumer Protection

Privacy

The mark reflects a considerable weakening of the privacy provisions in H.R. 10, which the Administration viewed as a good start but in need of improvement. Under the mark, it is difficult to ascertain what institutions, and therefore, what sharing of information, would actually be subject to notice and opt out requirements.

The problem goes far beyond the fact that the mark does not include restrictions on affiliate sharing of financial information. New exceptions and new definitions open wide loopholes beyond the weaknesses of the privacy provisions in H.R. 10.

Affiliate Notice. The mark fails to require financial institutions to provide consumers with disclosure before sharing customers' information with affiliates.

Affiliate Choice. The mark fails to require financial institutions to provide consumers with opt-out before sharing customers' information with affiliates. Just as customers would not expect a letter carrier to read their mail or record their correspondence, they do not expect a bank processing a check to record, store, and evaluate their personal behavior. Consumers should have a choice as to whether their financial institutions can use personal financial information to market non-financial information or to do behavioral and lifestyle profiling.

Significantly broadens affiliates exception. The new definition of affiliates is very broad, significantly increasing the types and number of companies that could be considered affiliates and thus not covered by the bill.

Invites regulators to create additional exceptions. Regulators are given the authority to establish additional exceptions to the notice and opt-out requirements, but not to enhance the privacy protections.

Joint Agreement Exception. The mark greatly expands the scope of activity that is exempted from the opt-out to include joint marketing arrangements with non-financial institutions – such as telemarketers or department stores – as well as between financial institutions – such as banks and unaffiliated insurers. This is supposed to level the playing field between conglomerates and small banks. Instead, it opens a loophole that undermines the entire privacy rule, allowing large organizations to market freely with other large organizations, with no choice for their customers regarding the use of their financial information.

A financial institution would not have to disclose the joint agreement to the consumer nor would it have to contract with the third party to ensure that the nonaffiliate maintains the confidentiality of the information.

In addition, the joint agreements no longer have to be between two financial institutions.

They can be between a single "independent" institution and <u>any third party.</u> Financial information can be freely shared with the whole economy under this expanded exception.

An "independent financial institution," as newly defined under the mark, far from being limited to smaller banks, could cover a wide range of financial institutions.

"Joint agreements," are defined in a vague manner that opens many possibilities for avoiding consumer notice and choice. A joint agreement is a contract to "offer, endorse, or sponsor" a financial product or service.

The disclosure of information under a joint agreement is also excepted from inclusion in the disclosure of an institution's general privacy policy.

Fair Credit Reporting Act. The mark would permit regulators to examine for compliance, but does not authorize rulemaking. This is a step back from H.R. 10, which would have enhanced existing protections for affiliate information sharing by allowing such rulemaking.

Inference that state laws would be preempted. Because subtitle B on pretext calling clearly provides that it would not preempt stronger state laws, the absence of a similar provision in subtitle A suggests that preemption is intended.

Preemption of stronger state laws should not be presumed, and the language should be clarified to this effect.

Limits on Redisclosure remain too weak to be effective. The provision provides very little limitation on redisclosure or reuse of information by third parties. Third party marketers are not covered by any of these provisions. If such a third party violates these provisions and discloses consumer information, there is no remedy or enforcement provided for in this bill.

There is no requirement that the unaffiliated third party or its affiliates need to provide consumer notice and opt out, nor is there any confidentiality requirement on any of the third parties. Furthermore, there is no mechanism for enforcement of the redisclosure provision. Thus, there is effectively little or no constraint on redisclosure or reuse of customer financial information by third parties and their affiliates.

As a result, a bank, insurance company, or securities firm could disclose its customers' financial information to a telemarketer for a marketing campaign and the telemarketer could subsequently share that information with its affiliate. Marketers would be free to disclose sensitive customer information with no confidentiality requirements.

Limited access to disclosures. Some important privacy information would be available only via Web sites. The mark would allow a financial institution to provide required disclosures about information sharing and privacy policies to be in electronic form. However, not all consumers have access to such electronic forms. If a bank chose to comply with this disclosure requirement by posting its information sharing notice on its Web site only, customers without Internet access would not be able to view or print these notices.

Investor Protections

Securities Consumer Protections: Investors need to be equally protected whether they purchase securities from a brokerage, bank, or other entity. The current mark has provisions that will harm the integrity of our markets and the securities law protections on which investors rely.

The bill contains significant loopholes enabling banks to sell securities to retail investors, without the critical sales practice protections of broker-dealer regulation. These critical areas include swaps and derivatives, private placement, and trust departments.

In addition, the safekeeping and custody exception in the mark would permit banks to provide any type of financial service through their custodial department, without securities regulation.

Other Consumer Protection Issues

Redomestication of Mutual Insurers: The mark includes provisions that allow for redomestication of mutual insurers, which fails to ensure fairness to policyholders in demutualizations.

State Consumer Protection and Non-Profit Health Insurer Conversions: The mark may preempt a number of state laws preserving the public's interest in the charitable assets of non-profit health care plans that convert to for-profit status. Thirty-five State Attorneys General have written letters on this issue. We agree that nothing in the financial modernization legislation should preempt these laws.

State Override: The mark includes the Senate provision giving the states three years to override the bill's consumer insurance protection provisions. We believe the federal rules should set a floor so that the states can strengthen, but not weaken, consumer protections.

* **Insurance Consumer Protections**. The mark does not apply the insurance consumer protection requirements to bank sales of securities. These protections include, for example, disclosure that the securities products are not FDIC-insured, restrictions on coercive practices, suitability requirements, and a grievance process for resolving consumer complaints.

* **Preemption of State Consumer Protection Laws on Sales of Credit Life Insurance:** The mark is vaguely worded in a manner that may preempt a broad range of insurance consumer protection laws, including laws that prohibit the practice of financing lump-sum, up-front credit insurance policies that, particularly when combined with

loan-flipping, may strip homeowners of their assets.

Compliance with Anti-Redlining Laws: The bill fails to include a provision originally in the House Banking mark that would require bank holding companies and their affiliates to comply with the Fair Housing Act. This simple provision mandates compliance with existing anti-discrimination law as a condition for engaging in new activities.

The Financial Services Act of 1999 - Banking and Commerce Issues

Unitary Thrift Holding Company. The transferability of existing unitary thrift holding companies is not addressed in the mark, but will be decided by the Conference Committee.

* Any bill acceptable to the Administration must limit transfers to non-financial companies.

Merchant Banking. The Administration's commerce and banking concerns related to merchant banking are:

* The mark fails to mandate, as the House bill mandated, that merchant banking investments are to be held *only* for a period of time necessary to dispose of the investment on a reasonable basis.

* the mark waters down the House bill's prohibition on bank holding company active day to day management of the companies held as portfolio investments, requiring only that the bank holding company "does not routinely manage or operate such company or entity."

* the mark fails to include the House bill's prohibition on bank lending to merchant banking affiliates or subsidiaries or the portfolio companies they control.

Complementary Activities. The mark does not require that activities that are complementary to financial activities remain small, as the House bill requires. The mark merely requires that they pose no safety and soundness problem -- an easy standard that would not prevent a material blurring of the line between banking and non-financial activities.

Notes from Gensler Call 10/22/98

Have + Maintain

(1) Chase or Hambrecht + Quist not

Citycorp against Solomon

Insurance

Companies

Absolute prohibition

Commence a new activity or open merge

Non-bank activity

Unsafely

(2) $250 mill / 5 years Lo Fa

4 years

Mgd. discrete diff any man

Louis excluded

(3) Sunshine

Narrowed a scope

Will + not mortgage — disagree or deny of underlying deal

or million or rate

Relieved to

Fail if required

deem have material effect on approval disagree

Null + void IF report is willful false + then can cond + null + void

Mortgage escrows

bail out

small children

Boy Scouts

House Bill + Civil Rig

~~Sus~~ $\boxed{\text{B--n A}}$

(1) F.. Hil

(2) P-rty n
sh-t-r F.

Set up + party - any in-n

Summary:

① Once 1 year for each grant

② Not cover all aspects

aspect model effect in term

exclusions: group not covered
- not controlled
- focus on 1 aspect

conduct + rapid process

③ If you do X, he finds

more effect or other pr

④ Time to focus on process

⑤ Produce 1 and repeat report

will, not fund to aspect
after has seen
return to
opp to apply

Firm

outside experts

Window

List

with person not connected in discussion

Feedback app

Under State Rules:

- Em power in his mem
- he could push vote
  just say
- Mayor Report: never
  This point: Chair next
- language is ambiguous: (Cannon some way it)
  let other people
  Chyn do

3 simple issues:

(1) As you know here in compli
Report: get to her expt

→ Need in mayor

(1) Most recent cnty close ⟷

(2) We would put targets: Burgh

(3) FED: and expt at which you'll do
Reports new look

Review CRA
actual perf →
dismay
or none of
perform

10-27-99

THE WHITE HOUSE

WASHINGTON

October 22, 1999

Copied
Sperling
Podesta

MEMORANDUM FOR THE PRESIDENT

FROM: GENE SPERLING

SUBJECT: NEC WEEKLY REPORTS

cc: JOHN PODESTA

New Markets: Following, our discussion with you on Thursday to finalize sites for your upcoming New Markets trip we have talked with the First Lady's office, Mayor Daley's office and have also begun to investigate possible sites in upstate New York and Southern Massachusetts. Seeing how Newark, NJ, seems to be firm as the starting point for your trip you should know that I have talked with several individuals, including Ray Chambers, David Stern, Commissioner of NBA, Bud Selig, Commissioner of the MLB, Bill Milliken, Head of Communities-in-Schools, and Art Ryan, Chairman and CEO of Prudential Insurance Company of America who are willing to work with us on meaningful, long-term projects for New Markets. Ray Chambers and I are working with the NBA to see if it is possible to have some form of NBA-wide announcement in time for the Newark trip. While that will not be possible with Major League Baseball, Bud Selig was enthusiastic about developing a partnership for New Markets over the next few months. Likewise, I am optimistic that we could develop a significant New Markets partnership for the Lawyers for One America group. On Friday, I spoke briefing at the monthly meeting of the Lawyers for One America group on how they could become involved in your New Markets initiative for the long-term. They have a number of good ideas and are very interested in creating a sustainable project. We are also working to develop a strong deliverable should Chicago be one of our final destinations. Congressman Rush called Thursday night from the hospital to find out if we wanted him to try and get Speaker Hastert to attend your Chicago visit. I told him that we would want to have Hastert there, but that it was still not clear whether Chicago would be one of our visits.

Taxes: Wednesday (10/20) the Senate Finance Committee by voice vote ordered reported a $8.5 billion paid-for tax extenders package. Recall that earlier this month, the House Ways and Means Committee reported a larger bill that was not paid for. The Ways and Means Committee scheduled for Thursday (10/21) and then scrubbed a markup of the Lazio-Shimkus Republican minimum wage and tax cut bill.

Financial Modernization: We actively sought to make clear late Thursday night and all day Friday the degree to which the tentative Conference agreement reflected a capitulation by Senator Gramm to the Administration's core CRA principles. We put out a Presidential Statement, and that was quoted in The Washington Post and The New York Times. Between Secretary Summers and me, we did CNN, CNBC and Fox News. Much of Friday was spent trying to overcome the natural suspicion of community and civil rights leaders about any "agreement" reached with Senator Gramm. While we expect that heat will continue from the left and we will face some criticism from some House Democrats, our efforts have been encouraging. Reverend Jackson and LISC both issues statements strongly supportive of the resolution. We expect others to follow on Monday, when the text is available. We have talked to Cathy Bessant, Sandy Weill, Jackson, Wade Henderson, LISC and Enterprise heads, and others. We are providing information and support to Minority Leader Gephardt and his staff to help them explain the agreement to the Democratic caucus. To be comfortable and help convince others, Gephardt and others want to see the bill text reflecting the agreement, which should be available by Monday.

Social Security: Throughout the week of 10/11, John Podesta, Larry Stein, and I met with Senators – among them Senators Levin, Conrad, Dorgan, and Moynihan – and found support for your submission to Congress of Social Security lock-box enforcement legislation in the week of 10/25. We expect, however, to receive some dissatisfaction from Senators Bob Kerrey and John Breaux, but that is unavoidable.

Child Labor Convention: At a hearing Thursday, Senator Helms expressed his support for the ILO Convention on the Worst Forms of Child Labor and said the Convention would be considered by the Senate Foreign Relations Committee on November 3rd. While he expressed skepticism that the convention would make a difference in the "most corrupt and impoverished countries," he said "we must do what we can do to try." He noted that negotiators had consulted regularly with the Committee and had ensured that the convention was consistent with U.S. law. Secretary Herman, AFL-CIO President Sweeney, and US Council for International Business President Tom Niles testified representing the three ILO sectors. Some Senators took the occasion to press for stronger linkage between labor rights and trade. Senator Wellstone specifically urged the Administration to push boldly for labor rights in the WTO. Senator Feingold pressed Secretary Herman for views on a possible child labor amendment to the Africa Trade bill.

Preparing an Economic Plan for East Timor: This week the NEC oversaw the preparation of working papers that lay out a strategy for building up East Timor's economy on its road to independence. East Timor presents special challenges because it is so poor. If East Timor were an independent country today, its average per capita income of $400 per year would make it the 6th poorest country in the world, about the same as Chad and Malawi. Over 80 percent of the government spending in the region represents "net transfers" from the rest of Indonesia—transfers that will disappear with statehood. Most of the people are subsistence farmers, but a few export coffee through Indonesian brokers. Eventually oil deposits off the coast might produce more lucrative cash flows, but for now they only bring in about $10 million a year. A joint NEC/NSC deputies meeting this week discussed what the framework of an economic action plan might look like. There is a need to make sure that there is a solid IMF/World Bank presence in East Timor as soon as these organizations can legally get involved.

Implementation of IFI Military Audit Provisions Could Prove Problematic for Nigerian President Obasanjo's Visit Next Thursday: Three weeks ago a law took effect that requires U.S. executive directors at the international financial institutions to vote against all non-basic human needs loans to countries that do not have procedures for their military spending to be audited by civilian authorities. The idea was that IMF and World Bank money should not go to

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countries that hide the extent of their military spending from the public. The Secretary of the Treasury has now set the audit standard and decided that 22 countries fail to meet it, including China and Indonesia. Secretary Summers has not yet decided whether to accept the recommendation of an inter-agency working group to also place Nigeria on the final "fail audit standard" list. With President Obasanjo of Nigeria scheduled to visit next Thursday and with our desire to offer him a "dividend for democracy," this raises the possibility of some diplomatic awkwardness. The NEC ran a deputies meeting on Thursday to address these issues. At that meeting it was decided that a higher level legal review was warranted to see whether the working group might have been overly stringent in setting its criteria. Treasury also agreed to explore with Senator Leahy, a key advocate of this legislation, whether some flexibility in implementation could be shown for countries that are in the process of upgrading their audit capabilities. The deputies will discuss this matter early next week to decide on the best strategy for the Obasanjo visit.

What exactly mean?

Electricity Restructuring: Chairman Barton has scheduled a markup of his electricity restructuring legislation next week. We have identified four significant criticisms of his bill: (1) it contains no market power provisions; (2) it codifies a recent court decision which makes it difficult for FERC to promote open transmission access; (3) it fails to promote sufficiently the development of regional transmission organizations; and (4) it is not green enough. Although there is no consensus among subcommittee members regarding the bill (even the Republicans), we believe that enough Republicans (and a few Democrats) will support the bill in order to move the debate to the full Commerce Committee. Barton, aware that Chairman Bliley will try to move to the left on the bill in full Committee, appears to have decided not to address the concerns of the Administration or Congressman Markey (a key Democrat on this issue and ~~cosponsor of the Largent-Markey restructuring bill~~) at the Subcommittee level. Bliley has committed to scheduling a full committee markup in January.

Seattle WTO: A Swiss informal "Friends of the Round" Ministerial is being held next Monday and Tuesday (Oct. 25-26) to discuss the revised draft declaration issued by WTO General Council Chairman Mchumo on the 19th. Roughly 25 countries (with representatives from all major regions) will attend the Ministerial in an effort to begin narrowing the differences. Ambassadors Barshefsky, Esserman and Hayes all plan on attending for USG. Your October 27th meeting with EU Commission President Prodi will have cooperation on Seattle WTO as the number one agenda item. NEC deputies agreed Friday to work with the EU to develop a common position that would encourage all countries to deepen and accelerate preferential tariff rates for LDCs.

Sanctions Reform: Next week, an Aschroft-like food and medicine sanctions reform bill may well be introduced and voted on. Aschroft announced at a press conference this week that Senate leaders had agreed to a vote the week of Oct. 24th. The bill is likely to be very similar to the Aschroft Amendment that was attached to the Senate version of ag approps by a 70-28 vote several weeks ago. The original Aschroft Amendment would have eliminated existing food and medicine sanctions (including Cuba) and prevent the Executive Branch from including such items in future sanctions regimes absent specific Congressional authorization or a declaration of war. The amendment was deleted in conference due to concerns over removing sanctions on Cuba. We share the goal of excluding food and medicine from sanctions having announced and implemented are own policy change that such items will be excluded absent a finding by you that our national interest requires otherwise. However, the Aschroft bill does not maintain sufficient

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Executive Branch flexibility to respond to various and rapid changing events (e.g. where a regime is denying food to a particular ethnic group or where we are in a state of hostilities without a declaration of war).

Africa Trade Bill: Cloture was filed at noon today (10/22) following yesterday's debate. The prospects are good for a vote to take place next Tuesday. Lael Brainard, Maria Echaveste, and Chuck Brain briefed the African diplomatic corps on the Hill at the request of Rep. Sheila Jackson Lee this past Wednesday to show visible support and to educate them on White House efforts underway to win passage of the bill. Representatives' McDermott, Kilpatrick, and Bernice Johnson also attended and gave brief yet convincing remarks.

Possible Trade Law Reform Amendments to Africa Trade Bill: Steel Caucus members are threatening to offer as amendments to the Africa Trade Bill legislation that would change our dumping and Section 201 laws in WTO inconsistent ways. We will fight such legislation on the grounds that passage of such measures would inflame our trading partners just as we are engaged in a heated battle to keep our dumping laws off the table in the new WTO round. We already have an industry-labor-Administration working group up and running pursuant to the Steel Action Program to review trade law reform legislation.

We are making progress on hurdles encountered to win Senate passage by strengthening our efforts to educate. As a result, the majority of the African American community is expressing its united support and enthusiasm for the bill. Moreover, we plan to meet with high-ranking African American religious and community leaders for a briefing on Monday followed by a bipartisan press conference on the Hill. So far, there are twenty-seven proposed amendments to the trade bill that we are working to develop positions on to head off potential procedural delays. However, the actions of Rep. Hollings are still unpredictable, and no one knows at this time whether or not he will use delay tactics when the bill is ripe for a floor a vote.

They have to work this out

International Debt Relief: Discussions are ongoing on both your appropriations request for $370 million in FY 2000 (with the remaining $600 million over the next three years) as well as the authorizing legislation in the House Banking and International Relations Committees. The authorizing Committees next week may mark up the implementing legislation for the Cologne Initiative, including the crucial authority for the US to support IMF gold sales of up to 14 million ounces. Treasury has been negotiating with Reps. Leach and LaFalce, seeking to convince them to accept our changes to their bill. We are making progress; however, a couple of issues remain outstanding. In particular, Democratic Members, who dislike IMF/World Bank conditionality, would like somewhat different and more general economic reform conditions to apply to USG debt relief than to the multilateral debt relief component of HIPC/Cologne Initiative; they would like to authorize but not require us to provide relief to more countries than those on the HIPC list if there were sufficient appropriations to do so; and they would like to ensure that IMF gold sale proceeds are used exclusively for financing debt relief. Treasury is attempting to negotiate acceptable language on these and other concerns. We understand that Leach and LaFalce are eager to mark up next week, and that the House International Relations Committee, which shares jurisdiction on the USG debt relief part of the package, would be likely to follow Leach's and LaFalce's lead.

ok

Air Traffic Control Reform: The conference committee on the FAA bill has begun to meet, but it is unclear if the House, which wants to take the aviation trust fund off budget, will be able to reach agreement with the Senate, which--like the Administration--opposes off budget. It appears very unlikely that conferees will address fundamental air traffic control reform in this bill. However, we believe it may be possible to achieve reform next year, once the airlines are out from under their obligation to support the Shuster bill. NEC staff is starting to work with CEA, OVP, OMB, Treasury and DOT/FAA to look at reform options, including privatization, for inclusion in your 2001 budget and state-of-the-union. My staff met this week with former Gov. Baliles, who chaired your commisison on the health of the airline industry and remains a vocal champion of air traffic control reform.

EU Hushkit Regulation: Dorothy Robyn on my staff will hold an NEC deputies meeting on Monday (Oct. 25) to consider next steps in our dispute with the EU over its so-called hushkit regulation, which limits the ability of certain older aircraft to operate in the EU despite their compliance with international noise standards. John Podesta and NEC staff met this week with representatives from United Technologies, Northwest and American Airlines, and they are pushing us to challenge the regulation under an international aviation treaty. However, that action could bring an end to our negotiations with the EU, which we believe are still bearing fruit. We will have talking points so that you can raise this issue with Prodi.

New Steel Numbers: Relatively good news this month. Steel imports fell 10 percent in September from August levels and remain 24 percent below the levels of September 1998. Looking at the first nine months of this year, 1999 steel imports are down approximately 14 percent compared to 1998, but are 9 percent above 1997 (1997 levels are the point of comparison for industry, as the surge began in 1998). Japan's imports fell by a third from August to September, and are down 45 percent this year compared to the first nine months of 1998, but are 34 percent above 1997 levels. Korean exports are off only 10 percent though September compared to last year, and 89 percent above 1997 levels. By contrast, overall imports from Russia have fallen 75 percent this year compared to 1998, and are off 66 percent compare to 1997. Wire rod imports dropped 24% from August to September, but are up 23 percent compared to September 1998 as imports continue at high levels as a precaution against a decision to impose trade relief in the Section 201 case.

March 17, 2000

TO: NEC PRINCIPALS

FROM: FINANCIAL PRIVACY WORKING GROUP

RE: PROPOSED FINANCIAL PRIVACY LEGISLATION

I. SUMMARY

Last year's financial services legislation (the "Gramm-Leach-Bliley Act" or "GLBA") includes important provisions to protect the privacy of sensitive consumer financial information. For the first time, consumers will receive notice about companies' policies for sharing information with affiliates and third parties, and have the right to "opt-out" of having their information shared with third parties (but not affiliates) for marketing and other purposes. However, the President promised at the GLBA signing ceremony, and again in the State of the Union, to propose legislation to provide individual choice before personal financial information can be shared with affiliated firms.[1]

The working group has developed a proposed legislative package on financial privacy. In addition to providing consumers with the right to opt-out of having their personal financial information shared with affiliated firms, the package would:

- Grant customers access to financial information that institutions collect about them and the right to have that information corrected, if it is inaccurate or incomplete;
- Restrict the use of medical information obtained from a financial institution's affiliate;
- Eliminate an exception in GLBA that allows banks to engage in joint marketing agreements for financial products without providing customer choice; and
- Make other minor improvements to GLBA, drawing on lessons learned through the rulemaking process.

Finally, in transmitting the package, the Administration would indicate that the Treasury Department will complete a GLBA-mandated study of financial privacy before the end of

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[1] "*Without restraining the economic potential of new business arrangements, I want to make sure every family has meaningful choices about how their personal information will be shared within corporate conglomerates. We can't allow new opportunities to erode old and fundamental rights.*" President Clinton, GLBA Signing Ceremony, November 12, 1999.

the year. In that study, Treasury will consider whether additional protections are necessary to address emerging technologies and information practices. (This leaves us a opening to propose further protections if we end up supporting either legislation or self-regulatory efforts imposing higher standards for on-line companies and want to ensure equivalent protections for financial information.)

The appendix provides a short summary of the views of various interested parties.

II. SUMMARY OF LEGISLATIVE PACKAGE

A. *Offer Consumers Choice Regarding Information Sharing Among Affiliates.*

Under current law, there are two major sets of restrictions on information sharing by financial institutions: the Fair Credit Reporting Act (FCRA) and the recently enacted provisions of GLBA.

The FCRA categorizes information into two types: (1) **application information**, which is information that a consumer provides on an application for credit or employment; and (2) **transaction and experience information**, which includes account balances, deposit and withdrawal amounts, the identity of payees and sources of deposits, information on what payments are made for, and summaries of any of the foregoing).

FCRA requires notice and opt-out before **application information** can be shared with affiliates. If application information is shared with a third party, the entity sharing the information becomes a credit bureau subject to a series of regulatory requirements.

Under GLBA, financial institutions' customers must be given the ability to opt-out before their **transaction and experience** information can be shared with third parties, subject to a long list of exceptions.[2] However, only notice must be given before such information can be shared with affiliated companies; consumers have no "choice" other than to take their business elsewhere.

Current law coverage is summarized in the chart below. In signing GLBA, the President pledged to revisit the chart's shaded box, implying that we might want to require notice and opt-out (as we had proposed the previous May) in this context as well.

[2] Exceptions include sharing: under "joint marketing" agreements; necessary to effect a transaction, for fraud prevention and risk management; to resolve consumer inquiries; with rating agencies, accountants, and auditors; with law enforcement; in connection with mergers and acquistions, and to comply with other laws or court orders.

	Transaction and Experience Information (Covered by GLBA)	Application Information (Covered by FCRA)
Shared with an Affiliate	[redacted]	Notice and Opt-out
Shared with a Third Party	Notice and Opt-out (with exceptions)	Institution sharing becomes a credit bureau subject to various requirements

Our new proposal would extend the opt-out choice available for third party sharing to the sharing of transaction and experience information among affiliated firms. As a rule, affiliated companies would not be able to share without offering an opt-out. However, the proposal would contain the same exceptions applicable to third party information sharing under GLBA (but not the joint marketing exception, as discussed below). Sharing with affiliates for law enforcement, data processing, and similar purposes would be exempt from the opt-out.

In addition, we propose to clarify a existing exception to ensure that sharing of information for risk management and customer service purposes are permitted without opt-out, as long as notice is provided. This would allow a credit card company, evaluating a credit limit increase, to consider that the customer has just defaulted on a small business loan to the company's bank affiliate. It also would allow an institution to produce and send consolidated account statements, covering insurance, securities, and other accounts in a single document.

We considered other options including: (1) requiring opt-out before sharing with affiliates only for certain activities (marketing and profiling) or only for the most sensitive information; (2) requiring opt-in before sharing with third parties, but not affiliates; or (3) requiring opt-in before sharing with third parties and affiliates. As a policy matter, the working group does not see a compelling need for opt-in before most information can be shared within financial holding companies. Many uses of such information can provide customer benefits, but inertia will lead only a fraction of customers to affirmatively opt-in. Some of us believe that sharing some types of information, or sharing for certain uses, might justify stronger protections like opt-in. However, given the largely rhetorical nature of this debate this year, we did not think it worth offering a complex proposal with various degrees of protection (both more and less protective) for different categories of information or uses. However, we do propose to indicate that Treasury will continue to study emerging technologies, leaving us an opening to argue for greater protections at a later time.

B. *Improve Consumers' Ability to Access and Correct Financial Information.*

Consumer groups and the EU have pushed us to grant consumers an unequivocal right of access to their financial information. In practice, consumers already have substantial access rights – financial firms are legally required to provide monthly account statements and make corrections where appropriate, and financial firms routinely honor requests for copies of historical records.

We propose to strengthen federal access rules by explicitly providing consumers the right to access personal financial information that institutions collect about them, and to have that information corrected if it is inaccurate or incomplete. The customer would have to cover the reasonable cost of the search, and there would be an exception for proprietary information such as credit scoring models.

C. ***Prevent Unauthorized Use of Medical Information Obtained from an Financial Institution's Affiliate.***

In May 1999, the President called for limitations on sharing medical records within financial holding companies. We sought to ensure that a financial institution would not make credit decisions based on medical information about the customer obtained from an affiliate without the customer's permission. In response, House Republicans attached a deeply flawed medical privacy amendment to the Financial Modernization bill. It actually would have *reduced* the protections provided by current law and HHS regulations on medical privacy. We were concerned that this would give the Congress a chance to say they had addressed medical privacy without tackling the more comprehensive medical privacy legislation that we supported. In the House, we sought and won an instruction to conferees that the medical provision be stripped; and it was removed in conference.

Some Banking Committee Democrats and Republicans criticized us for stripping the provision. They argued correctly that HHS regulations cover only certain insurance providers, and would not protect medical information held by life, auto, some disability, and property & casualty insurers affiliated with banks.

This year, we wanted to close this gap with a limited provision that would not reopen debate on medical privacy more broadly. We propose to say that a financial institution or subsidiary may not receive, obtain, or consider medical information from an affiliate, unless it requires the submission of and considers the same specific medical information about *every* applicant for a financial product or service. In addition, in order to receive even this limited range of information, the institution would have to obtain the customer's opt-in consent before any sharing could occur. Finally, the proposal will clearly state that nothing in this law or in the GLBA supercedes the provisions of the Health Insurance Portability and Accountability Act or regulations promulgated under it.

This provision will likely be popular, as consumers particularly fear misuse of this type of data, and it is easy to explain the risks. It also would close a genuine loophole in existing law. And it would please Democrats like Reps. LaFalce and Vento, who acceded **reluctantly** to Administration wishes that medical privacy be dropped from GLBA. HHS and some Democrats, while generally supportive of the proposal, have lingering concerns about our ability to limit the way Congress addresses the issue and fear that the standards that apply generally to medical data might be lowered. They are also concerned that "fixing" life insurance or other records in the financial bill would reduce the chances of including those entities in future medical privacy legislation.

D. ***Remove Joint Marketing Exemption.***

The third-party opt-out provisions of GLBA provide an exemption for financial institutions that join forces in "joint agreements" for purposes of marketing financial products and other services through third party marketers. This exception was intended to level the playing field, allowing small financial institutions (without affiliates) to take advantage of information-sharing opportunities that larger financial conglomerates could do, without opt-out, by sharing amongst their affiliates. However, in fact, it is badly written and broad enough to allow large and small institutions to avoid GLBA's protections in many cases.

Since we propose to require an opt-out before inter-affiliate sharing – leveling the playing field between larger and smaller institutions -- there is little justification for retention of the joint marketing exemption. When Congress takes up this issue, however, we may be pressed to consider some alternative relief for small banks.

E. ***State Preemption.***

GLBA includes a Sarbanes amendment providing that nothing in that law shall preempt state privacy laws that go further. However, the FCRA contains an explicit preemption of state regulation of information sharing within a "corporate family" – i.e., affiliate sharing – until 2004. This does not prevent states from providing access or limiting third-party marketing. Even for affiliate sharing, states can still enact restrictions provided they do not take affect until 2004.

As a result, the financial services industry's greatest anxieties about privacy restrictions currently focus on the States. They are concerned not only about *strict* regulation, but also *inconsistent* regulation – the possibility that a nationally active bank would have to process data under 50 different state regimes. If additional federal privacy protections are ever adopted, industry will demand state preemption. Many Hill Democrats and consumer groups recognize that this deal probably would be part of additional federal privacy legislation, but none believe we should concede the point now.

Our proposal would be silent on preemption, thus leaving the Sarbanes amendment's general preemption, and the FCRA exceptions, in place. This is consistent with our general policy that we want to leave in place the ability of states to provide greater protections, but would not preclude us from accepting an agreement at a later time that included some form of federal preemption. We considered whether to close the FCRA exception loophole, but no privacy advocates were urging us to do so and doing so might open the debate on broader preemption prematurely.

F. *Prevent Abuses of Bankruptcy Trustees Financial Information Databases.*

Bankruptcy trustees collect and hold a great deal of sensitive financial information regarding those with whom they have trustee relationship. Much of this information is required to be made public by law, in court records and elsewhere, to assist interested parties in pursuit of legitimate claims against debtors in bankruptcy proceedings. Other information, such as payment schedules for debtors to creditors in a bankruptcy workout, is not part of the public record.

Private bankruptcy trustees are considering proposals to aggregate and sell this information to third parties ostensibly to facilitate creditor monitoring of repayment under Chapter 13 plans. While the trustees appear to want to be responsible, the commercial distribution of large databases of non-public information to those without a direct interest in a particular bankruptcy claim raise privacy and other policy issues. Other bankruptcy records contain detailed financial information. Making even these public records available over the Internet has significant privacy and security implications. Appropriate protections should be put in place before any such information is available electronically. We are proposing a study to be conducted by the Executive Office of the U.S. Trustees (DoJ), OMB, and Treasury.

G. *Make Financial Institutions Responsible for Misrepresentations of Their Privacy Policies.*

The initiative will clarify that an institution will be considered in violation of the law and subject to sanctions if it fails to honor ***any*** aspect of in its stated privacy policy as disclosed to consumers under GLBA, whether or not that particular aspect of the privacy policy is required by GLBA or any other federal law. Under current law, banks are not covered by the Federal Trade Commission Act's general prohibition on unfair and deceptive trade practices.

We also are still considering whether additional enforcement mechanisms should be included in our proposal. Options include heightened oversight by regulatory authorities, enforcement authority for State Attorneys General, and a private right of action. The last would be highly controversial, but we have insisted on it to protect medical privacy.

H. *Ensure That Consumers Can Use Privacy Policy Notices for Comparison Shopping.*

Our proposal would clarify that privacy notices must be provided to individuals upon request, and as part of any application for a financial service, to enable consumers to make informed decisions based on comparisons of those policies before the time a customer relationship has been established. The GLBA is unclear as to the timing of initial notices, and does not mandate that they be included with application materials.

I. *Clarify the Definition of Non-Public Personal Information.*

Our proposal would clarify that ***all*** information collected by an institution in connection with the provision of a financial product or service, including Social Security numbers, is to be covered by notice and opt-out requirements for ***both*** affiliate and third-party information sharing.

J. *Ensure That Secondary Market Institutions Cannot Transfer Sensitive Data.*

Our proposal would repeal the blanket exception in GLBA for Fannie Mae and Freddie Mac, while retaining specific exceptions to allow sharing as part of secondary market activities, e.g., securitizations. Thus, Fannie and Freddie would not be permitted to construct profiles of homeowners and sell that information to third parties such as home equity lenders.

K. ***Provide Better Enforcement for Pretext Calling.***

GLBA prohibits the practice of "pretext calling," -- obtaining of information about individuals through the use of false statements and other deceptive tactics. It also authorizes criminal penalties for offenders, but grants enforcement authority only to the FTC. Our proposal would extend enforcement authority to State Attorneys General.

L. ***Close Loophole in Re-Use Provision.***

The re-use provision in GLBA is supposed to hold a recipient company to the same standards as the company that transfers the data. A drafting error appears, however, to allow a loophole if a company first transfers the data to an affiliate. The data might then be transferable without the re-use restrictions. We would close the loophole.

APPENDIX A
VIEWS OF INTERESTED PARTIES ON FINANCIAL PRIVACY LEGISLATION

Rep. Markey/Senator Shelby. Markey and Shelby formed an unlikely left-right alliance over privacy issues in the S. 900 conference, and are still working together on the issue. Last year they introduced the "Consumers' Right to Financial Privacy Act," which provides notice and ***opt-in*** for all information sharing, requires institutions to give consumers access to all information about them, and prohibits institutions from denying services to customers that opt out of information sharing.

Upon passage of last year's bill, Markey said, *"The White House really pulled the rug out from under consumers by agreeing to weak privacy protections in the banking bill."* Shelby's comments were similarly negative, and there are no indications that either will back away from their public stands. Indeed, the two recently founded a bipartisan, bicameral "Congressional Privacy Caucus" to push their legislation. Shelby has a few Republican allies in this effort, including Rep. Joe Barton (TX).

Other Democrats. Minority Leader Daschle announced the formation of another privacy group, the Senate Democratic Privacy Task Force, February 9. The group is chaired by Sen. Leahy, and is designed to be more of an educational effort than a legislative task force. Leading pro-privacy Democrats in the Senate include Bryan, Sarbanes, and Leahy. Bryan is the most vocal of these, and is the sole co-sponsor of the Shelby bill. Sarbanes has introduced privacy legislation before, but has been hesitant about pressing the issue – his interest is significantly staff-driven. House pro-privacy Democrats include Dingell, Waxman, and Hinchey.

Senator Gramm. Gramm strongly opposes Congressional efforts to legislate privacy policy. He opposed the provisions in S. 900, and in a February 3 interview said, *"This is an issue that is being driven by polls and politics. I am not going to let the Information Age be killed off before it is ever born."* Gramm has the support of all of his Committee Republicans except Shelby on the issue.

Industry. Financial services firms have generally opposed legislative privacy protections, and fought to dilute the provisions contained in the GLBA. They can be expected to oppose any new privacy bill. However, two factors may make them more amenable to legislation than they have been in the past.

- Thirty or more states may consider financial privacy legislation this year. The prospect of having to comply with 50 different state requirements is far more daunting to most firms than a federal rule, and many may be willing to trade tougher federal protections for preemption of state laws.

- Some major firms are already providing at least notice and opt-out for affiliate marketing already (Citigroup under an agreement with the Federal Reserve, Chase Manhattan under a settlement with the New York Attorney General, Washington

Mutual and other Washington State thrifts voluntarily). They may thus be able to accept a federal rule that codifies practices similar to those they already have in place.

Consumer/Privacy Advocacy Groups. Advocates generally favor much stronger privacy protections, and complained loudly that the GLBA provisions did not go far enough. The Treasury and the White House were accused by some of settling for too little. Their strongest criticisms focused on the omission of affiliate restrictions, the exception for joint marketing agreements, and the failure to grant consumers a right of access.

THE WHITE HOUSE

WASHINGTON

March 28, 2000

MEMORANDUM

TO: NEC PRINCIPALS

FROM: FINANCIAL PRIVACY WORKING GROUP

RE: SUPPLEMENT ON PRIVACY OF BANKRUPTCY INFORMATION

SUMMARY

This memorandum supplements the March 17 memorandum to NEC Principals regarding Proposed Financial Privacy Legislation, and replaces the section entitled "Prevent Abuses of Bankruptcy Trustees Financial Information Databases." In the interim, the working group has continued to explore options to address concerns about the lack of privacy protection for sensitive financial information gathered in the course of bankruptcy, especially in light of pending proposals for broad distribution of such data, without adequate privacy controls. The working group recommends: (1) we include in our financial privacy package a narrow substantive provision limiting use and disclosure of certain "non-public" bankruptcy data; (2) we announce that the President has directed federal agencies to conduct a study of appropriate privacy protection of "public record" and "non-public" bankruptcy data; and (3) we continue apparently successful efforts to get the Bankruptcy conference committee to make changes to language in the House and Senate bills that could be harmful to financial privacy.

THE PROBLEM

Individuals filing for bankruptcy put their financial information in a number of hands. Public record bankruptcy court filings must include a wide range of sensitive financial data, including: bank and other account numbers, a social security number, itemized income (e.g., salary, income from property, alimony, government assistance); and expenses by category (e.g., rent, food, medical expenses, installment payments). In addition, non-public case administration data is collected by private trustees – private individuals engaged to administer bankruptcy cases (e.g., liquidate assets or collect and distribute payments under a repayment plan). The trustees are required to make this information available to any creditors who file a claim and other "parties in interest." Nothing limits trustees' ability to share such information with others as well.

Consider the following privacy concerns. A growing number of courts are exploring or actually making judicial records available on-line. Previously, "public record" information was accessed only by people who took the time to go to the courthouse to get a record, i.e., people most often with a real stake in the matter. Now, public record information is increasingly available with the click of a button to curious friends and neighbors, employers, marketers, and predators looking for those most likely to be lured by scams. While this problem is true of all public records, bankruptcy records raise greater concerns because they contain particularly sensitive financial information and because of the special vulnerability of the debtor population.

Another concern is raised by an effort of the private trustees to make the non-public case administration data available more efficiently in a centralized database accessible to bankruptcy creditors across the country. One model the trustees are exploring is to create a trustee-owned "National Data Center" (or "NDC"). When DoJ's Executive Office for U.S. Trustees (EOUST) expressed concerns about privacy, the trustees expressed a willingness to build some protections into the NDC system, but the EOUST's authority to regulate the use and reuse of such information is limited. As a result, with this project, the private trustees could ultimately *and legally* broadly disclose debtors' non-public case administration data in bulk and for profit.

Finally, the Administration shares the concern that there is insufficient statistical information available about bankruptcy cases, making policy judgments difficult. However, as described below, the current bills go too far by urging public access to personally identifiable information not needed for policy analysis, further weakening privacy protections for debtors.

RECOMMENDATIONS

Narrow, Substantive, Privacy Proposal in Financial Privacy Bill. Currently, EOUST is working on privacy guidelines that private trustees would be required to adhere to in the NDC project, and more generally in their handling of debtor information obtained in the course of case administration. However, the EOUST's jurisdiction is limited to the private trustees and does not allow them to restrict use of the non-public data once it is in the hands of creditors, information clearinghouses, and other third parties.

As a result, we propose to include a narrow, substantive protection in the Administration's financial privacy bill. This proposal would prohibit the private trustees from disclosing non-public case administration data, except generally to parties in interest under EOUST guidelines, or with the debtor's affirmative, written consent. It would also prohibit any entity from using or disclosing such data for purposes that are unrelated to case administration, unless again the debtor provider written consent.[1] We believe that this proposal fits well with the Administration's overall effort to apply stronger legally enforceable privacy rights to individuals' sensitive financial data -- rights implicated in a bankruptcy case as much as in a financial institution.

Administration Study. We propose that the President direct the U.S. Trustees, Treasury,

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[1] In accordance with current law and practice, under our proposal, a creditor would be able to examine payment information to other creditors in order to determine the equitable administration of the case.

and OMB, in consultation with the Judicial Conference, to conduct a study of privacy issues raised by bankruptcy data, including its release in electronic form, to be completed by the end of the year. In announcing the study, we could show the special sensitivity of data in an actual public bankruptcy filing and ask whether we think it fair that the price of filing bankruptcy is to have such information available to the whole world. For example, John Q. Public owes creditor Bank ABC, account number 3578912, a monthly mortgage of $2,500; he owes Morristown Cars-Are-Us, for his account number 3425, $360 in car loan payments; he also owed $500 monthly in alimony. John Q. Public earns $30,000 in salary.

Revisions to Language in Bankruptcy Legislation. Both bankruptcy bills include "sense of the Congress" language that public record information from bankruptcy filings should be made available electronically. In addition, the Senate bill includes language making it a duty of private trustees to provide case administration information to a non-profit entity via the Internet. Finally, the House bill contains a provision protecting the trustees from liability in the case of unintended errors in the release of information. These issues were buried in bill text and not widely noticed until after both bills passed.

We are working with Senate Democrats to include a caveat that the release of public bankruptcy data be subject to appropriate privacy and security safeguards as determined by the EOUST and the Judicial Conference of the United States. We are also working to strike the language regarding trustees' *duties* to provide their case data and the liability exemption provision, arguing that such provisions are at best premature before an appropriate plan and EOUST guidelines are established.

THIS FORM MARKS THE FILE LOCATION OF ITEM NUMBER 1
LISTED IN THE WITHDRAWAL SHEET AT THE FRONT OF THIS FOLDER.

THE FOLLOWING PAGE HAS HAD MATERIAL REDACTED. CONSULT THE WITHDRAWAL SHEET AT THE FRONT OF THIS FOLDER FOR FURTHER INFORMATION.

CONSUMER FINANCIAL SERVICES WORKING GROUP

4:00 pm

Sarah Rosen, NEC
Jonathan Orszag, NEC
Thomas Kalil, NEC
Paul Weinstein, DPC
Mary Smith, DPC
Thomas Freedman, DPC
Nicole Rabner, DPC
Diana Fortuna, DPC
Doug Elmendorf, CEA
Joe Minarik, OMB
Alan Rhinesmith, OMB
Edward Brigham, OMB
Alice Veenstra, Examiner, OMB
Fran Allegra, DoJ
Rick Carnell, Treasury
Hug ~~Doug~~ Baer, Treasury 2-6-62 [redacted]
Joan Affleck-Smith, Treasury 7-11-37 [redacted] Michael Bylsma 5-21-53 [redacted]
Mark McClellan, Treasury 6-26-63 [redacted]
Julie Williams, OCC 5-5-50
Chris Lewis, OCC 12-27-60 [redacted]
Amy Friend, OCC 0-16-58 [redacted]
Ellen Seidman, OTS [redacted]
Ken Ryder, OTS 1-13-43
Eric Berg, OTS
Bill Magrini, OTS [redacted]
David Medine, FTC 7-15-53
w Peggy Twoig, FTC
Lucy Morris, FTC
Becky Burr, Commerce
Larry Campbell, Commerce
Eric Biel, Commerce
Pam Gilbert, CPSC
Arnold Grundeman, USDA
George Greenberg; HHS
Marcy Wilder, HHS
Donald Oellerich, HHS
Paul Weech, SBA
Jean Veta, Education
_______, OPL
Roger Ballentine, OLA
Robert Weiner, WH Counsel
Maria Eschaveste, CoS (FYI)

David Envel
1-21-55
[redacted]

Tim Burniston
2-29-55
[redacted]

Paul Robin
4-15-60
[redacted]

NEC PRINCIPALS MEETING
FINANCIAL PRIVACY
AGENDA
April 3, 2000

I. Summary of Working Group Recommendations (see memo attached)

- Give consumers right to opt-out of affiliate sharing;
- Give consumers the right to access and correct their financial information;
- Restrict the use of medical information obtained from an affiliate;
- Eliminate GLBA exception that allows banks to engage in joint marketing agreements for financial products without providing customer choice;
- Propose no changes to current GLBA and FCRA preemption, leaving states free to impose more restrictive requirements, except as to affiliates prior to 2004;
- Consider including some enhanced enforcement mechanism (special regulator responsibilities, state AGs, or private right of action – **open issue**); and
- Make other improvements to GLBA, drawing on lessons learned through the rulemaking process.

II. Discussion: On affiliate sharing, this is largely what is expected. Are we comfortable with where this would position the Administration?

	Third Party Sharing	Affiliate Sharing
Industry	Opt-out	Notice only
LaFalce and Vento ('99)	Opt-out	Opt-out for marketing; otherwise notice
LaFalce and Vento ('00)	Not on record; probably Opt-out	Not on record; probably Opt-out
Safe Harbor	Opt-out	Opt-out (no agreement on financial)
Senate Democrats (not Schumer)	Opt-in	Opt-out
Markey and Consumer Groups	Opt-in	Opt-in
Proposed Medical	Opt-in	Opt-in
Children's On-line	Opt-in	Opt-in

Notes:

- We also would propose an access/correction requirement and elimination of the joint marketing "loophole" from GLBA, which would please Democrats and consumer groups.
- We would indicate continuing Treasury study of emerging practices, leaving an opening to come back to argue for higher standards for "profiling" and like practices involving financial information, if we ultimately support more aggressive legislation in on-line arena.

Fin Priv

April 21, 2000

MEMORANDUM

TO: NEC PRINCIPALS

FROM: FINANCIAL PRIVACY WORKING GROUP

RE: FOLLOW-UP ON FINANCIAL PRIVACY PROPOSALS

SUMMARY

During the NEC Principals meeting on April 3, 2000, you discussed the possibility of adding to our proposal another requirement: a financial institution must get affirmative consent (opt-in) before sharing any payee information with an affiliate or third party.[1] Before deciding whether to include this element, you asked the working group to explore several questions, which are discussed in detail below. We also advise you below (see issue 5) of a change we have made to our earlier recommendation on privacy in bankruptcy. We are also preparing a brief assessment of the Congressional outlook on opt-in proposals which will be sent separately.

1. What are the options for an opt-in requirement for especially sensitive financial information, and what information would be covered?

The working group wants to highlight three options in this area. <u>Option one</u> would be to exclude any opt-in requirement from the proposal. <u>Option two</u> would require an opt-in before a firm could share specific information about: (a) to whom the customer has made a payment by check, credit card, debit card, or other payment mechanism ("payee information"); (b) from whom the customer has received a payment or transfer of funds ("payor information"); and (c) for what purpose any of these payments were made. <u>Option three</u> would also cover the profiles derived from this specific transaction information under the same opt-in. These options are discussed in greater detail below.

<u>Option 1: No Opt-In Requirement:</u> Under this option, the core substantive proposal in our financial privacy legislation would be to provide opt-out choice for both affiliates and third-party information sharing. There would be no special protection for payor/payee information or for profiles derived from such information. This would match what the President has said would be included in the Administration's proposal, i.e., choice for affiliate-sharing, but would go no further.

<u>Option 2: Payor/Payee Information:</u> This option would provide consumers with opt-in choice before their transaction-level information could be shared by a financial institution. During the last Principals' discussion, the conversation focused on payee information. However, the working group believes that equally sensitive information could be contained in payor information (sources of income or deposits into your accounts). Imagine, for example, a consultant or an independent contractor whose bank account provides a complete record of her clients. We could articulate no justification for distinguishing between payee and payor information. If the decision is made to proceed with either option 2 or option 3 (the opt-in-based options), we believe that it should cover payor as well as payee information.

This option is consistent with the substance of the recent proposal of Senator Shelby, a leading proponent of financial privacy legislation. If the Administration's opt-in proposal covers only the payor/payee

[1] Interestingly, Senator Shelby introduced a new bill last week that would do effectively the same thing. Entitled the "Freedom from Behavioral Profiling Act of 2000," it would require an opt-in before any financial institution could share payee <u>or payor</u> information with an affiliate or a third party.

information, we should be careful not to oversell it as a limit on behavioral profiling. It is interesting to note that Senator Shelby billed his recent legislation as the "Freedom from Behavioral Profiling Act of 2000." He said, in introducing his legislation: "[F]inancial institutions would only be allowed to buy, sell, or otherwise share an individual's behavioral profile, if the institution had disclosed to the consumer that such information may be shared and the institution has received the consumer's affirmative consent to do so." Yet, as we read the bill, it would not require opt-in before profiles inferred from the information were shared or sold – only before specific transaction information itself is shared or sold.

Option 3: Payor/Payee Information and Profiles: A more difficult decision is posed by whether to require opt-in before sharing only specific transactional information or also to require opt-in before sharing the results of analytical models (i.e., profiles) derived from that transactional information. (See the Appendix for the modification to the legislative language that would accomplish this broader purpose.)

If the restrictions apply only to payor/payee information, we would prohibit a credit card company from sharing, for example, without your affirmative consent, the fact that you contributed to far-right wing political groups, purchased a book on gay marriage, or paid your ex-spouse only $100 a month in child support. However, they would be able to share, absent opt-out, profiles that describe you as right-wing extremist sympathizer, gay, or divorced. These examples are intentionally sensitive; many firms would be reticent to profile in these areas. Many people probably would have less objection to the profiling if firms were simply describing an individual as a Redskins fan, avid tennis player, frequent traveler, or aficionado of fine wines and cigars. However, it may be impossible legislate a workable distinction between "benign" and "non-benign" profiling categories. Note that under this option, we also include an anti-circumvention provision designed to preclude financial institutions from disclosing transaction-level information in the guise of a profile.

If the restriction also requires opt-in before sharing profiles, that would be a far bigger step than restraining the sharing of payor/payee information, as it would constrain existing industry practice. Credit card companies, for example, create profiles of individuals' purchasing behavior and use that information in target marketing (everything from bill inserts to phone solicitations). They share the profiles with affiliates and sometimes sell the profiles to third parties. A few years ago, there was a firestorm when the press reported that American Express was considering selling the specific payor/payee information. The focus of the criticism was on sharing of "the raw data." American Express quickly retreated, and asserts they have no plans to share the more specific information. There has not been similar criticism of their continued practice of developing, using, and selling profiles based on consumer purchasing behavior.

If the Administration requires an opt-in for sharing payor/payee information without covering the profiles, some might argue that it would not adequately protect individuals against transfers of this sensitive information. Under the proposal, payment service providers would not be able to sell the fact that an individual made seventeen trips to Europe last year and stayed at particular hotels. They would, however, be able to "profile" that individual as a "frequent high-end European traveler," and sell that profile to others for marketing purposes.

2. Would the Administration be treating financial institutions differently than other firms, especially other on-line firms? Could we defend our policy as consistent?

Generally speaking, financial institutions and businesses whose activities are "financial in nature" are covered by the privacy restrictions in current law and under our new proposal. Thus, for the most part, comparable financial activities will be regulated similarly. However, there are some circumstances in which similar information could be collected by non-financial firms not covered by this statutory regime (as we would amend it). We also discuss below issues of consistency between the Administration's approach to privacy in the on-line world and the financial privacy proposal.

Covered Activities: The Gramm-Leach-Bliley Act (GLBA) and our new proposal cover all institutions engaged in financial activities, which are defined clearly in statute and regulation. Traditional financial institutions (banks, thrifts, securities firms, investment companies, insurance companies, and credit unions) engaging in activities "financial in nature"[2] are subject to enforcement by their respective financial regulator. In addition, other firms engaging in activities "financial in nature" are also subject to the privacy provisions.[3] Companies that engage in activities financial in nature, but are not traditional financial institutions, fall under the jurisdiction of the FTC.

The FTC's proposed rule states that it will view an entity engaged in an activity financial in nature as a financial institution only if it is "significantly" engaged in that activity. The FTC uses the following example: a retailer that directly issues its own credit cards to consumers will be considered a financial institution; one that merely establishes a deferred payment or layaway plan will not. The agency has sought comment on whether the term "significantly" should be more precisely defined. The FTC staff have indicated their intent to give consumers of like products like privacy protections. That is, the purchaser of a service that falls under the definition of "financial" should be protected to the same degree whether that service is obtained from a regulated bank or a non-traditional provider.

To help analyze the issue, we considered the case of AOL. AOL says that it does not collect information about the purchases that its customers make from merchants at the AOL site. They perceive that it would be seen as an invasion of privacy to keep track of their customers' purchases when using the service (of course they do keep track of their customers' browsing habits). They collect purchase information only for, products purchased from AOL itself, such as shirts bearing the AOL logo. However, if AOL were to collect that information, it is not clear whether they would be considered a financial institution under GLBA. AOL is now considering creating a "digital wallet" product. Customers could choose to put their credit card, home address, and other information into an AOL-maintained server to help speed transactions with e-merchants. In that case, AOL would expect to provide a log of such purchases to their customers, similar to a monthly credit card statement. These "digital wallets" may become a major payments system for e-commerce, and we believe that such services clearly should and would be "financial in nature" and therefore covered by the financial privacy rules.

Concerns have been raised that the payor/payee approach could create a situation in which credit card companies may have an advantage because they would possess more information than other market participants regarding a customer's transactions. If customers follow usual preferences and a low percentage of them opt-in to sharing of transaction-level financial data, credit card firms could have a competitive advantage in targeting communications to a single individual for marketing purposes.

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[2] Activities that are "financial in nature" are defined as:

1. **Activities specifically named in the statute,** including lending and other banking activities; insurance underwriting, annuity, and agency activities; securities underwriting and dealing; merchant banking; and financial or economic advice or services.
2. **Any activity that the Federal Reserve Board had determined to be "closely related to banking or a proper incident thereto"** prior to the enactment of the GLBA. These activities include financial data processing, acting as a certification authority for digital signatures, and check cashing and wire transmission services.
3. **Any activity that a bank holding company may engage in outside of the U.S., as authorized by the Federal Reserve,** such as management consulting services; operating a travel agency; or organizing, sponsoring, and managing a mutual fund.

The Act also sets up a process under which the Federal Reserve and the Treasury may jointly determine that additional activities are "financial in nature" or "incidental to [a] financial activity" in order to accommodate future developments in financial products.

[3] Exempt from coverage under the privacy title are: companies to the extent they engage in activities subject to the Commodity Futures Trading Commission's jurisdiction; the Farm Credit System institutions and Farmer Mac; and government-sponsored enterprises that engage in securitization or secondary market activities, as long as they do not sell or transfer nonpublic personal information to a nonaffiliated third party.

However, credit card companies will face competition from other institutions that collect substantial amounts of transaction data. Competitors include other payment service providers, companies like Amazon.com that collect detailed information on a variety of online purchases, and internet "portals" that collect extensive browsing information. In addition, since our proposal would bar companies from selling payor/payee information without consent, any competitive advantage to payment service companies must be weighed against the assurances consumers will have that their payment information will not be distributed to those with whom they did not entrust such information.

__Comparison with Non-Financial Privacy Policies:__ The Administration has generally taken the position that the more sensitive the information, the greater the privacy protection should be. We therefore supported legislation that requires an opt-in before sharing medical information or gathering information from children on-line. Current law also requires opt-in before sharing telephone numbers called, video rentals, release of student records, records of cable television viewing, government records, and release of drivers' records for marketing.

Regarding on-line privacy, while we have not proposed legislation for other on-line activity, we have urged self-regulation that provides for notice and opt-out choice for activity on Internet websites. In addition, the FTC and Commerce are in negotiations with the "Network Advertising Initiative" (NAI) about possible approaches to self-regulation of the practices of on-line profilers, who collect information about web surfers and select advertisements based on the surfers' behavior. They have taken the position that these practices raise special concerns (compared with data gathered at a merchant that the surfer chooses), because the surfers do not select the profiler and do not necessarily know of the profiler's activity. The agencies have made clear that, if the NAI does not agree voluntarily to practices that are sufficiently protective of privacy, they might support legislation.

While these negotiations are on-going, any code that results would likely require: (1) **opt-in** for any linking of a person's identity with on-line information that was gathered previously when surfers did not know of the profiler and could believe they were acting anonymously; (2) **notice and opt-out (likely "robust" opt-out,** with the option highly visible to surfers) for linking of surfing information in the future with the surfer's identity. In addition, a recent draft submitted by NAI contained a prohibition on profiling medical and financial information.

There are arguments that the Administration's policy on online privacy and options 2 and 3 of the financial privacy proposal -- each of which involve opt-in choice -- may not be comparable. Concerns have been raised that the opt-in provision in the financial proposal will make it more difficult to sustain our self-regulatory approach, which has generally called for notice and opt-out choice. This concern is stronger still if the opt-in covers profiling (option 3), and not just payor/payee information (option 2). Because the distinction between opt-out and opt-in is so significant, we would need to be able to explain the discrepancy in policy approaches. Another argument of inconsistency is based on the fact that the Administration's online privacy policy has been to support self-regulation, whereas here, we propose financial privacy legislation.

There are also arguments that our online and financial privacy policies are consistent, as follows: Option 1 presents the strongest argument for comparability. It provides for opt-out choice in both industry sectors. For option 2, one argument is that there are no similar transactions in the online world as the payor/payee transactions that would be covered in the financial privacy proposal. Another argument is that the payor/payee information is most sensitive and merits greater protection, as evidenced by the special protection that American Express and AOL provide voluntarily for such information. For option 3, the argument would be that the Administration adopts a view that financial profiling information is most sensitive -- like payor/payee information -- and therefore merits the greater, opt-in protection. Finally, for all options, current law and the Administration's proposal would treat a payment account or other "financial in nature" activity the same whether it is conducted on-line or on paper.

3. **Would announcing this legislative proposal, or the addition of an opt-in for payee/payor information, harm our prospects for completing negotiations with the EU on the "safe harbor"?**

At the first Principals' meeting, the Working Group was asked how the proposal overall, and a possible opt-in for payor/payee information, would affect the safe harbor talks with the European Union (EU). The Working Group has tentatively concluded that, while the privacy package as a whole could have an effect on negotiations with the EU, the addition of an opt-in for payee-payor information or for profiles probably will not change the course of those discussions, whatever they may be, significantly.

The most significant parts of the Administration's proposal from a safe harbor perspective are those dealing with affiliate sharing and access. Administration officials negotiating the safe harbor have envisioned for some time that financial services firms would need to comply with GLBA as well as affiliate sharing and access rules in order to have safe harbor benefits. With the release of this new privacy proposal, we would better align our position regarding the protections required domestically with the protections that we said were required for adequacy under the safe harbor. This is consistent with the position that U.S. officials took in EU negotiations in March. We should understand, however, that the industry will likely object to new requirements on affiliate sharing and access for both domestic legislation and safe harbor purposes.

Regarding the proposals to require opt-in before sharing payor/payee information and profiles, no similar opt-in is required in the EU. Under the EU Data Directive, opt-out is generally required before marketing uses. Opt-in is required for certain sensitive information, such as medical, ethnicity, and union membership data. But financial information is *not* considered sensitive under the Directive. We are not aware of any special privacy rules in the EU that are focused on the sorts of financial payments that may be covered by our opt-in proposal.

4. **Would our privacy proposal prevent financial conglomerates from achieving the synergies which the Administration and others argued would flow from breaking down Glass-Steagall barriers between banking, securities, and insurance? Was information sharing a key element of those benefits?**

While financial services firms may have sought modernization legislation, at least in part, in order to make it easier to benefit from information sharing within financial conglomerates, this was not their primary argument on its behalf. Nor was it a major focus of Administration arguments, where we emphasized ***greater choice*** for consumers, farmers, and small businesses. We also said that modernization should result in ***lower costs*** to consumers as more financial service providers compete for customers, and that it should ***improve access*** for under-served consumers by encouraging new competitors to find profitable opportunities in previously overlooked markets.[4] However, in an October 5, 1999 speech Secretary Summers specifically mentioned the importance synergies and information sharing in financial modernization legislation in connection with the need for greater privacy protections. He said:

> "Financial privacy has gained much greater prominence as an issue since the last Congress. Much of the benefit of financial modernization is synergy, and part of that synergy is derived from the sharing of information from developing innovative products to relieving customers of the burden of reintroducing themselves to an institution each time they do business. Nonetheless, revelations about financial service industry practices have come as a shock to policy makers and many consumers, who thought that financial services firms preserve the confidentiality of personal customer information. Our challenge is to protect the privacy of consumers while preserving the benefits of competition and innovation."

[4] We checked the 1997 Rubin and Hawke testimony before House Banking and House Commerce (and the Exchequer speech and Key Points of the Treasury plan released in May '97), as well as 1998 and 1999 Senate and House testimony, and could find no references to cross marketing or synergy benefits.

Regardless of which option is selected, we believe that our plan strikes the right balance. While an opt-in requirement would provide greater protection for the most sensitive financial information, we would allow financial institutions to relieve their customers of the burden of needing to provide the same information to multiple affiliates. The Administration's proposal would expressly exempt sharing of information with affiliates "in order to facilitate customer service, such as maintenance and operation of consolidated customer call centers or the use of consolidated customer account statements, other than for marketing purposes."

5. Privacy in Bankruptcy: Revised Recommendation

We continue to recommend that the President announce that he has directed DOJ, Treasury, and OMB to complete a study of privacy and access issues in bankruptcy data before the end of the year. We also believe we should continue to work to eliminate provisions harmful to privacy in the current House and Senate bankruptcy bills. However, we are withdrawing the recommendation that we announce one substantive new provision now, as part of the broader financial privacy package. There are too many questions that we need the study to resolve before we can feel confident in the policy proposal.

APPENDIX

SECTION 102. LIMITATION ON PAYOR AND PAYEE PROFILING

Section 502(b) of the Gramm-Leach-Bliley Act (15 U.S.C. 6802(b)) is amended to read as follows:

"(b) DISCLOSURE OF PAYEE AND PAYOR INFORMATION--

"(1) NOTICE AND OPT IN.—Notwithstanding subsection (a), if a financial institution provides a service to a consumer through which the consumer makes or receives payments or transfers by check, debit card, credit card, or other payment mechanism, the financial institution shall not disclose to an affiliate or a nonaffiliated third party—

(A) the identity of any person or entity to whom a consumer has made, or from whom a consumer has received, a payment or transfer by check, debit card, credit card, or other payment mechanism;

[(B) information about a consumer derived from the information described in paragraph (A);] or

"(C) the goods or services for which such payment or transfer was made.

"(2) EXCEPTIONS.—

"(A) A financial institution may disclose the information described in paragraph (1) to an affiliate or a nonaffiliated third party if such financial institution —

"(i) has provided to the consumer a notice that complies with section 503; and

"(ii) has obtained from the consumer affirmative consent to such disclosure and such consent has not been withdrawn.

"(B) This subsection shall not prevent a financial institution from disclosing the information described in paragraph (1) to an affiliate or a nonaffiliated third party for the purposes described in subsections (f)(1), (2), (3), (5), (7), (8), (9), or (10).".

April 27, 2000

MEMORANDUM

TO: NEC PRINCIPALS

CC: SALLY KATZEN
DAVID BEIER

FROM: FINANCIAL PRIVACY WORKING GROUP

RE: FINAL ISSUES ON FINANCIAL PRIVACY

We urgently solicit your views on two remaining issues: (1) whether we should describe the narrow opt-in proposal as involving "personal spending profiling" or use another term (see options below): and (2) whether to include an additional provision that would preclude sharing transactional information or characteristics derived therefrom involving especially sensitive issues (e.g., sexual orientation, religion, political views). We also attach the final legislative language that we have developed for the opt-in proposal. ***We ask that each of you share your reaction to this memo with your staff immediately (or contact Sarah Rosen Wartell directly at 456-5386). We will compare notes and determine whether or not a principals' phone call should be scheduled for this evening.***

I. USE OF THE TERM "PROFILING"

Principals discussed on Monday whether to use the word "profile" in describing what is covered under the new opt-in provision for spending or earning information, including the list of purchases made via credit card, debit card, and similar payments mechanisms or characteristics derived therefrom. During the call, we agreed to try the word "profile" with limiting adjectives. Staff has agreed that "personal spending" is the best modifier to describe what is covered (although technically sources or income are also covered), as in "requiring an opt in for personal spending profiles or portraits." (Staff have agreed on legislative language that does not include this term. (See III below.) The only question is how we describe what the language does.)

In the call, we also agreed to discuss the issue with the Commerce Department, which has the lead on Internet privacy, where "online profiling" has become a term of art for the activity of companies like DoubleClick. Commerce is seeking a "robust opt-out" rather than "opt-in" those firms. Commerce, through General Counsel Andy Pincus, strongly prefers *not* to use the word "profiling" for reasons described below. (The best alternatives we could come up with are "personal spending habits" or "personal spending portraits.") David Beier and Sally Katzen agree with Commerce, and Peter Swire leans in the same direction. Treasury has expressed a preference for using "profile"but could live either way. Sarah Rosen Wartell, and Tom Kalil believe that we can manage the real problems raised by using the term "profiling" if we are exceptionally careful and clear in the background paper that we give to the press, Hill, groups, and industry. We seek final guidance from Principals.

In short, the problem is that the term "profile" is used to describe the practice we seek to limit (sharing info or characteristics of a specific person) but also used to describe practices we do not want to affect (sharing lists of people that have specific characteristics). Thus, the use of another, less well-known term might lead to misunderstanding of what we are trying to do; but use of the broader term could also lead to the conclusion that our proposal does more than it does. The latter problem could lead to problems when we subsequently announce the self-regulation agreement with the on-line Doubleclick-like industry and people argue that we have already said that "opt-in" is appropriate for "profiling." *Interestingly, both*

Karen Tramontano and Loretta Ucelli thought that most Americans do not know what "profiling" is and preferred the term "personal spending habits."

<u>The case for "personal spending profiles":</u>

- The word "profile" has political resonance and has been widely used in privacy debates.
- Legislative passage is highly unlikely this year, so nuances are less important and the clarity of our public message is more so.
- None of the other available terms is particularly compelling. Treasury staff, for instance, think that financial firms' opposition might be even greater if we require opt-in for a vague term like "personal spending patterns" which could be read to mean information used for risk management purposes (like unusual spending that prompts a call to ensure the card was not stolen) or other current industry practices.

<u>The case for "personal spending habits" or "personal spending portraits":</u>

- Several of the staff who also work on Internet privacy, and especially on the DoubleClick industry issues, have had the same negative reaction to using "profile." The vulnerability will come when the press says: "The Administration now favors opt-in for profiling." We will be exposed in the near term, when the Doubleclick industry privacy code is announced in a couple of weeks. That code will include a robust opt-out rather than opt-in. We will also be exposed in the long term on Internet privacy, when people ask why we favor opt-in for some profiling but oppose any legislation for profiling done of web surfers.
- The best argument for using the term profiling is also the best reason not to use it. Its political resonance stems from the public's broader expectations about the word's meaning.
- Because our financial proposal covers only a subset of financial profiling (allowing, for instance, the American Express stuffers), privacy advocates will criticize us for over-promising.
- Because industry engages in some form of profiling in a wide variety of settings, from credit card stuffers to telemarketing activities to e-merchants studying browsing patterns, many parts of industry may react negatively to the broad-sounding announcement of requiring opt-in for personal spending profiling.

DECISION: __________ ***"Personal Spending Profiles"***
__________ ***"Personal Spending Habits"***
__________ ***"Personal Spending Portraits"***
__________ ***Other***

II. PROTECTION FOR ESPECIALLY SENSITIVE INFORMATION

In the Principals' discussion on Monday night, Staff was asked to draft an option for requiring opt-in (or a ban on) sharing or profiling based on especially sensitive information. We provide below pros and cons for inclusion of such language; however, ***staff are unanimous in recommending <u>not</u> to include the provision in the package for the reasons set forth below.***

Staff's initial draft of this provision would require opt in for "any list or profile that identifies the consumer by -
(1) race;
(2) religious affiliation;
(3) sexual orientation;
(4) political affiliation; or
(5) medical condition."

Other candidates for inclusion might include: color, national origin, sex or marital status, or handicapped status. As for the other personal financial profiling, nothing would "prevent a financial institution from transmitting individualized information in order to identify the customer on an aggregate marketing list."

The analogous language in the Equal Credit Opportunity Act states that "it shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction-- (1) on the basis of race, color, religion, national origin, sex or marital status, or age." If we decided to go further with this provision, we would need to consult with DOJ.

In favor of including the provision:

(1) The law contains other anti-discrimination statutes that serve as analogies for this sort of limit on profiling. Categorizing individuals by group status such as race is noxious and legal rules can deter the bad actors.

(2) The anti-discrimination categories are traditional categories for defining "sensitive" information. Because we have generally sought to have stricter privacy rules for "sensitive" data, these categories are natural ones to consider including.

(3) This Administration strongly opposes discrimination, and this provision would send that message in a context where it would be hard for companies to defend their practices if they in fact were marketing based on the prohibited categories.

Against including the provision:

Although it is theoretically attractive to limit these sorts of noxious uses of information, arguments against doing so include:

(1) Some of the categories in traditional antidiscrimination statutes are widely used and accepted in the marketing context. For instance, marketing lists may target either men or women. Age is used for many marketing uses (would you want to receive the promotions received by a teenager?). Marital status and similar household information can be relevant for many marketing campaigns. The list used for ECOA may thus be over-inclusive.

(2) The list of categories used for ECOA may also be under-inclusive. Some especially sensitive information from a checking account may include political affiliation and sexual orientation. These categories have not usually been included in antidiscrimination legislation, and their inclusion here may draw a good deal of attention to this provision.

(3) For much of the most noxious behavior, some other law will probably often cover the activity, such as ECOA or the prohibitions on discrimination in forming contracts.

(4) The effect of this prohibition may most heavily fall on the most benign uses of such data, such as marketing of products that would be of particular interest to members of a group. Opting in to such uses may be unlikely because it would seem to be volunteering to be the victim of discrimination, even if the uses are economically beneficial.

(5) Several people have expressed concerns that including the antidiscrimination language could distract attention away from the privacy aspects of the proposal and into the different arena of civil rights legislation.

Decision: __________ *Do not include any provision*

__________ *Include a provision limiting any list or profile that identifies the consumer by the following characteristic [LIST THOSE YOU WANT COVERED]:*

III. FINAL LANGUAGE FOR OPT-IN PROPOSAL

The working group has agreed that the following language best reflects the concept for which we are requiring opt-in; however, lawyers still need to integrate this language into the section that describes the mechanism of opt-in.

RESTRICTION ON THE TRANSFER OF PERSONAL SPENDING PROFILES.

(a) If a financial institution provides a consumer with payment services through a check, debit card, credit card, or other similar instrument, that institution shall not, unless the consumer affirmatively consents (opts-in), transfer to any affiliate or nonaffiliated third party--

(1) an individualized list of that consumer's transactions or an individualized description of that consumer's interests, preferences, or other characteristics; or

(2) any such list or description constructed in response to an inquiry about a specific, named individual;

if the list or description is derived from information collected in the course of providing that service.

(b) Paragraph (a) shall not apply to the transfer of aggregate lists of consumers, consistent with [cross-reference the opt-in requirement].

April 29, 2000

COMMENCEMENT ADDRESS AT EASTERN MICHIGAN UNIVERSITY

DATE:	April 30, 2000
TIME:	12:50 p.m. – 2:45 p.m.
LOCATION:	Ypsilanti, Michigan
FROM:	Gene Sperling

I. PURPOSE

To announce a new legislative proposal to strengthen further the financial privacy of American consumers.

II. BACKGROUND

Rapid changes in technology and the vast increases in access to information that they make possible are enormously important to our future prosperity, but they also pose challenges to protecting personal privacy. In the past, your administration has taken a number of steps to ensure that technological innovation does not undermine privacy:

- **Electronic Bill of Rights:** In 1998 Vice President Gore announced an Electronic Bill of Rights, calling for private sector leadership where possible, legislation when necessary, responsible government handling of personal information, and an informed public.

- **Children's On-line Privacy:** The Administration worked with Congress to pass the Children's Online Privacy Protection Act of 1998. Rules went into effect this month to ensure that web sites aimed at children will not gather personal information except with the consent of the parents.

- **Medical Privacy:** Last year, the Clinton-Gore Administration announced historic proposed rules that would legally guarantee the key privacy protections: notice of data uses; consent before records are used for non-medical purposes; patient access to records; proper security; and effective enforcement. Final rules will be issued later this year.

- **Genetic Discrimination:** In February, you issued an Executive Order that prohibits federal agencies from using genetic information in hiring and promotion. You also called on the Congress to ensure that these same rights apply to employees in the private sector and to individuals purchasing health insurance.

- **Government Privacy**: All Federal agencies now have privacy policies clearly posted on their web sites, and we are making privacy impact assessments a regular part of the development of new government computer systems.

The financial services industry has changed dramatically in recent years, due to greater integration of banking, securities and insurance firms, new technologies that speed and expand access to information, and growing reliance on electronic payments systems (credit cards, debit cards, and even so-called digital wallets, which are on-line accounts that pay for purchases and bills) instead of cash. Such innovation has helped provide consumers with added convenience, lower prices, and more choices. The challenge is to take advantage of these benefits without threatening privacy.

The proposal you announce today aims to protect the financial privacy of American consumers, fulfilling the promise you made on November 12, 1999 when you signed historic legislation modernizing the financial system. While that bill took significant steps to protect the privacy of financial transactions, you made clear that the protections were not strong enough and directed the NEC, Treasury Department, and Office of Management and Budget to develop a new legislative proposal.

That proposal -- announced today and to be sent to Congress next week -- contains the following key elements:

- **Consumer Choice:** Consumers should have meaningful choice – the opportunity to opt-out -- before a financial services firm can share their private financial data with anyone. Last year's financial modernization legislation granted important rights to opt-out of information sales to telemarketers and other unaffiliated firms. Today's proposal extends those protections to information shared within financial conglomerates. The plan also closes an unnecessary exception for "joint marketing" from last year's bill. We will preserve, however, financial firms' ability to share the information that they need to develop new products and manage their risks, subject to appropriate confidentiality and reuse limitations.

- **Enhanced Protection for Especially Sensitive Information:**

  Affirmative Consent Before Sharing Medical Information: A consumer applying for a loan or other financial product should not have to worry that the lender is making decisions based on personal medical records received from an insurance affiliate. The Clinton-Gore plan will assure that companies would not gain any special access to insurance medical records by being part of a financial holding company. The consumer would be required to affirmatively consent ("opt-in") before any financial firm could receive medical information from a life insurance company or other affiliate.

  Affirmative Consent for Personal Spending Information: Just as we do not expect a postal worker to read our mail, we do not expect a bank processing our checks or credit card payments to take our most sensitive financial information and share that information with others. Under the Clinton-Gore plan, a financial firm will not be permitted to transfer individualized, personal spending habits (where we spend our money, where we earn our money, and what we buy) unless a customer affirmatively consents.

- **The Right to Access and Correct**: As financial conglomerates collect more and more data about us, it is increasingly important that consumers have the ability to review that information and correct material errors. Expanding on a protection already provided for credit reports, the Clinton-Gore plan would allow a consumer to ensure that firms are not deciding whether to offer them products or special services based on mistaken information about their financial status.

III. PARTICIPANTS

Pre-Event Briefing in Air Force One

- Maria Echaveste
- Gene Sperling
- Terry Edmonds
- Sarah Rosen Wartell, NEC
- Undersecretary Gary Gensler, Treasury

Speaking Program:

- **YOU**
- Professor Gary Evans
- Professor Glenda Kirkland
- President William Shelton
- Secretary Slater

IV. SEQUENCE OF EVENTS

- **YOU** arrive at Convention Center in Ypsilanti
- President William Shelton of Eastern Michigan University greets you
- All proceed to a photo receiving line of 25 people located just offstage
- When receiving line is finished, Professor Gary Evans announces you and Sec. Slater to the Convention Center audience from offstage

  Audience: About 8,000 students and families. Besides the Administration officials traveling with you from Washington, VIPs in the audience include former Governor Blanchard and Mayor Dennis Archer of Detroit.

- Professor Glenda Kirkland sings the national anthem
- Prof. Evans makes brief remarks and introduces President Shelton
- President Shelton makes brief remarks and introduces Sec. Slater
- Sec. Slater makes brief remarks and introduces **YOU**
- **YOU** deliver remarks
- President Shelton confers upon you an honorary degree in public service by placing a medallion around your neck

FINANCIAL PRIVACY PROPOSAL
QUESTIONS AND ANSWERS
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16. *Opt-in for Medical Information:* How does the financial privacy proposal protect medical records within financial holding companies?
17. *Opt-in for Medical Information:* The sharing of medical records within holding companies was a contentious issue last year during consideration of the financial modernization bill. The Administration opposed the medical privacy provisions in last year's bill and they were dropped at your insistence? What has changed?
18. *Opt-in for Medical Information:* Does this proposal mean that there is no longer any need for medical privacy legislation?
19. *Joint Marketing and Other Exceptions:* You say you are closing loopholes. Which exceptions have you eliminated?
20. *Enforcement:* How would this bill improve enforcement of financial privacy protections?
21. *Redisclosure and Reuse:* What effect would this proposal have on the ability of authorized recipients of information to reuse the information for their own purposes?
22. *Preemption:* How would this proposal preempt or otherwise affect state law?

<u>Comparison to Other Bills</u>

23. How does the Clinton-Gore financial privacy proposal differ from the other major privacy bills before the Congress?

Overall Message

- The President is fulfilling his commitment to press Congress to provide greater protections for the financial privacy of American consumers. [He pledged to propose legislation as he signed last year's Financial Modernization bill and again in his State of the Union.]

- The President believes that consumers should have the right to control how their personal information is used.

- The central principal of the Clinton-Gore plan: the more sensitive the information, the greater the protections to ensure that consumer is in control.

- Public interest in privacy protection will only continue to grow. The momentum is all one way. Those who assume the American people will wait for protections they view as essential, do so at their peril.

Timing and Political Prospects

Question 1: Why is financial privacy legislation needed now?

- ***We must assure that consumers can enjoy the substantial benefits of technology and recent market changes with the same level of confidence in the financial system that they had before. An integral part of maintaining consumer confidence is maintaining adequate privacy protection.***

- We are in the midst of three significant changes in the financial services sector: a technological revolution, industry consolidation and a move from cash to greater reliance on electronic transactions. These changes have brought greater choice, lower costs, and more efficient services.

- Last year's financial modernization legislation was an important first step toward ensuring that financial privacy keep pace with the rapid changes in the market place. However, as the President said when he signed the bill and later in the State of the Union, additional steps are needed. This bill fulfills his promise to put forward a new plan to provide assurance to consumers.

Timing and Political Prospects

Question 2: Industry argues that we should wait and see how the privacy provisions of the Financial Modernization bill work. Those regulations are still under development. Why not wait and see?

- The Financial Modernization bill only took the first step. But we know today what we need to give consumers' confidence in the financial system – control over how their information is used.

- It is clear that consumers need to have the right to choose whether their information is shared with affiliated firms or third parties. There is no compelling reason that choice should apply in an uneven way as it does today.

- Further, the sensitivity of information about your detailed spending habits or medical care requires immediate action. ***The pace of technological advances – and thus the pace of information sharing – accelerates every day, and we should act to protect the most sensitive information immediately.***

- Firms are just now really beginning to take advantage of the new opportunities to affiliate made possible under last year's bill. They will be building large data warehouses of information about consumers in each of their affiliates. Isn't it better that the rules of the road for such information sharing is established now, before firms sink enormous sums into systems that will need to be redesigned?

- Finally, last year's legislation contained inconsistencies and certain problematic provisions -- targeted in this new proposal which the regulatory process has identified but cannot correct without further legislation. These problems need prompt attention to make the statute work effectively.

<u>Timing and Political Prospects</u>

Question 3: Senator Gramm has made clear that legislation will not move this year? Why does this proposal matter?

- Predictions about the fate of privacy legislation are made at one's peril. The public interest in this issue is only growing. Momentum for further legislation is mounting. The American people may demand that their Congress acts to protect their financial privacy.

- When the President first announced on May 4, 1999, his support for legislation to adopt financial privacy protections, some said it would never happen then and that the Financial Modernization bill would contain no privacy provisions; yet only months later, Congress passed and the President signed a bill that contained important new protections – albeit only a first step.

- This President will be active until the last day of his Presidency working to meet the needs of Americans and pressing Congress to do the right thing. With this new proposal, the President will help build momentum for legislation.

__Timing and Political Prospects__

Question 4: Last year's bill called for a two-year Treasury Department study of information sharing between affiliated firms, yet the new proposal takes action on the issue before the study is complete. Isn't this proposal premature?

- Our work on the study has informed this proposal. But we know that the question of information sharing among affiliates needs to be addressed now and shouldn't wait.

- The ongoing study will address several issues related to affiliate sharing practices and technologies, and will be extremely useful in informing both future regulatory implementation, and future legislative action on these issues.

- Although Congress gave Treasury 2 years to complete the study, we plan to conclude it this year, in order to better information legislation and implementation of these proposals.

Relationship to Financial Modernization Legislation (Gramm-Leach-Bliley Act)

Question 5: Information sharing is one of the most powerful synergies driving affiliation between financial firms. Doesn't your privacy proposal undermine the very purpose of Financial Modernization that you so actively supported last year?

- We believe that the benefits of affiliation are fully consistent with increased privacy protection.

- Last year's modernization bill allowed broad affiliation among financial companies, to increase efficiency in the industry, increase the choices available to consumers, and help institutions remain internationally competitive.

- Our firms will specifically be able to share information to serve their customers better through things like consolidated customer service centers and all-in-one monthly statements.

- When it comes to choice, institutions will prove to customers that they will use their information appropriately and truly for their benefit. We believe that our proposal will not inhibit the operations or growth of our financial firms, and that the choice of how information should be handled rightfully belongs in the hands of consumers.

Relationship to Financial Modernization Legislation (Gramm-Leach-Bliley Act)

Question 6: What are the gaps in last year's Financial Modernization legislation that this proposal would fill?

- This bill provides greater protection for consumers, and greater certainty for financial institutions, by filling gaps and clarifying key inconsistencies in the existing statute.

  - ***Closing the Joint Marketing Loophole:*** This proposal closes the "joint-marketing" exception that would have allowed a firm to share a list without consumer choice if they were jointly marketing products with another firm.

  - ***Earlier Notices***: In addition, consumers would get privacy notices and choice earlier (upon application or request), so that she could effectively comparison shop on privacy policies. Current law appears to only require that these be provided when a customer relationship is established.

  - ***Eliminating Exceptions:*** Unnecessary special exceptions for certain financial institutions will be closed. This bill eliminates those special exemptions, and treats financial institutions equally.

  - ***Strengthening Enforcement***: The bill also strengthens enforcement authority. Under existing law, institutions that are not regulated by a financial (bank, insurance or securities) regulator are subject to FTC enforcement. The bill strengthens the penalties that the FTC can seek and provides a "second set of eyes" for these firms, by granting new authority to State Attorneys General. It would allow them to pursue actions in coordination with the FTC against persons who violate the privacy laws and regulations under this bill.

  - ***Limiting Reuse:*** Finally, current law does not preclude those who are transferred information (without consumer choice) for authorized purposes from reusing the information for their own profit. The proposal would close that gap.

Relationship to Internet Privacy

Question 7: Is the new financial privacy proposal consistent with the Administration's position on online privacy?

- Yes. The Administration's longstanding position has been to encourage self-regulatory efforts by industry in the on-line world. We have also consistently stated that legal protections are required for especially sensitive information, such as medical, children's on-line, ***and financial records.***

- For medical records, this year will see historic, final rules that will legally guarantee key privacy protections.

- When children go online, the new rules under the Children's Online Privacy Protection Act ensure that web sites must get verifiable parental consent before the sites can gather children's personal information.

- For financial records, the President said, when signing the financial modernization bill last November, that the new law "takes significant steps to protect the privacy of our financial transactions." The President also said that the bill did not go far enough, and he promised to announce a new legislative proposal to complete the unfinished business. The proposal today, once enacted, would do just that.

Relationship to Internet Privacy

Question 8: Would the proposal handle financial information online and offline any differently?

- No. For these activities, the rules would apply identically to online and offline behavior. For instance, the rules would apply in the same way to information from a credit card purchase made in person or over the Internet.

- As under current law, most of the financial privacy proposal would apply to activities that are "financial in nature." The special opt-in before sharing detailed descriptions of personal spending habits applies to any firm providing a payment service (checking account, debit card, credit card, or digital wallet) whether on-line or off-line.

<u>Relationship to Internet Privacy</u>

Question 9: The new proposal requires customer <u>opt-in</u> for descriptions of personal spending habits, while the Administration has supported <u>opt-out</u> for Internet privacy. How do you explain this difference?

- The Administration believes that the details of your spending habits is especially sensitive information and deserves the more careful protection of the opt-in. The Administration also believes that less sensitive marketing activities should continue to be subject to an opt-out, both for financial institutions and for the on-line world generally.

- The President's proposal would apply an opt-out for the sharing of financial information in order to include a customer on an aggregate marketing list. This sort of opt-out is consistent with Administration policy for on-line commerce, where we have encouraged companies to provide at least an opt-out for sharing of customers' information.

- In both settings where opt-out is required, individuals must have clear notice of how their information will be used, as well as an effective choice to say no to uses of their information of which they do not approve. In both settings, the information is being used to provide an entire group of consumers with a service, in contrast to the especially worrisome practice of singling out individuals for special scrutiny based on examination of particularly sensitive information.

Relationship to EU Negotiations on a Safe Harbor

Question 10: How will the Administration's new proposal affect the safe harbor talks with the European Union?

- It shouldn't effect those talks. The safe harbor talks focus on consumers in Europe, while the focus of the proposed legislation would be on American consumers.

Background:

In March, the U.S. Department of Commerce and the European Commission announced a "tentative agreement" on the safe harbor approach for all sectors except financial services. That tentative agreement will be considered by the Member States in late May, with the intention that the agreement will be in place for the US-EU Summit at the end of May.

Because the regulations under the financial modernization act are not yet final, the EU and U.S. will continue working together with the goal of bringing the benefits of the safe harbor to the financial sector. Neither side anticipates problems with interruptions in data flows while they continue their good faith efforts to resolve these issues.

The Safe Harbor process will create a framework for transfers of personal data from the EU to the US. Companies that sign up for the safe harbor will be considered to have "adequate" privacy protections under European law. For such companies, agreeing to a set of common-sense privacy principles will assure that trade can proceed free from the threat of data blockages. Eliminating this threat to trans-Atlantic trade means jobs for Americans.

The safe harbor approach is also a milestone for the Administration's approach to e-commerce. The approach highlights the role of self-regulatory organizations on the Internet. Companies can agree to meet the standards set by these self-regulatory groups, which we believe can greatly reduce the need for cumbersome legal regulation of the Internet. In this way, the privacy approach in the safe harbor talks can serve as a model for flexible approaches in other e-commerce areas, including consumer protection in a global Internet. In addition, the safe harbor talks are an example of constructive action involving the US and the European Union on a complex trade issue.

Questions About Proposal Details: Consumer Choice and Affiliate Sharing

Question 11: What does the bill do to improve consumer choice? Can firms share with affiliates without consumer choice?

- Last year's legislation granted important rights to opt out of information sales to telemarketers and other unaffiliated firms ("third parties"). This proposal extends those protections to information shared with "affiliates" within a financial conglomerate.

- Under current law, these conglomerates can include everything from a bank to a data processor to a travel agency. Consumers dealing with one firm would not reasonably expect that information about them would be spread so widely.

- In addition, last year's legislation does not ensure that consumers will receive notice of a financial institution's privacy policies and practices early enough to make meaningful comparisons between institutions.

- In order to make comparison shopping easier, the proposal clarifies that consumers should be able to receive a firm's privacy policy upon request, or with an application for a product or service -- not just before they are about to sign on the dotted line.

Questions about Proposal Details: Consumer Access

Question 12: Are the access and correction provisions really necessary? Don't existing laws (like the Fair Credit Reporting Act) adequate?

- With all the important information about you that your financial firms may collect, not merely from its own records, but from affiliates and third parties, it is important that consumers have the ability to know what the firms know and ensure that decisions about what products to offer you and on what terms are not influenced by incorrect information.

- For example, if a bank learns from its insurance affiliate that, because of your driving record, you are in a high risk car insurance pool, and may choose to offer you higher priced credit services as a result, you should have the ability to know what they know and make sure it is right. Similarly, banks may not report bounced checks to credit reporting agencies, but their credit card company may not offer you their best deal on credit card rates if they think you bounce checks. If that information is wrong, you should be able to correct it.

- Assuring individuals the right to see their financial records and correct mistakes will empower ordinary individuals and reduce the risk that important mistakes will creep into the new holding companies' databases.

- The principle that individuals should have access to important information about themselves is built into American law and practice in many settings. The Privacy Act of 1974 ensures that Americans have access to information held about them in federal government files. The right to access is incorporated in the well-known OECD Privacy Guidelines, approved by the United States Government in 1980, as well as in the privacy practices the Administration has encouraged in the online setting.

- The law does provide some access and correction rights for financial records. When credit histories contain incomplete or inaccurate data, a person can be turned down for a job or for a mortgage or other loan. For this reason, the Fair Credit Reporting Act of 1970 includes strong assurances that individuals will be able to see their credit history and correct any mistakes. However, it does not cover all the information that a financial firm might get about you from affiliates or other sources.

Questions about Proposal Details: Consumer Access

Question 13: Won't the new access rules be burdensome for industry?

- No. In many instances, financial services firms already provide detailed customer account statements that let consumers see their important records. Where financial services firms already provide effective access and correction, the new provision should not be burdensome.

- The provision also states that individuals will have access to their records that are reasonably available to the institution. Institutions will not have to disclose confidential commercial information, will be able to recoup a reasonable fee for providing access to a consumer's financial information, and will not have to create any new records.

Questions About Proposal Details: Opt-In for Personal Spending Habits

Question 14: Why has the Administration chosen to support opt-in for descriptions of personal spending habits?

- A central theme of the Administration's privacy policy is that more sensitive information should be treated more carefully. We believe that the information included in the detailed descriptions of spending habits, such as a list of every purchase made on a person's credit card, is truly sensitive information.

- Consumers should be able to use a credit or debit card, or write a check, with confidence that their financial institution will not release this detailed personal information without consent. Similarly, consumers should know that their list of purchases will not become a target for private investigators or others who want to use people's payment history as a database to search.

- Just as we don't expect a postal worker to read our mail, we don't expect a bank processing our checks to take our most sensitive financial information and then sell a highly personal description of our personal spending habits to outsiders for marketing.

- Consumers have little choice but to rely on payment systems for their everyday life. It is hard to carry out their household affairs without a checking account or credit or debit card. And these systems are often the only way to make a purchase over the telephone or in the rapidly growing area of on-line commerce. As Americans use these payment systems more and more, Americans should have confidence that their payment history will be treated confidentially. The price of having a credit or debit card should not be to have every purchase made with that card available to outsiders unless the customer specifically requests otherwise.

Questions About Proposal Details: Opt-In for Personal Spending Habits

Question 15: Last year's legislation gave consumers the right to opt out of having their financial information shared with firms that were not affiliates of their financial institution. How does the opt out requirement work in conjunction with the opt in requirement for especially sensitive information?

- This bill extends the consumers' right to opt out to include sharing among affiliates.
  - Before a financial firm can transfer an aggregate list of customers for marketing or other purposes, each consumer on the list will have had a chance to *opt out* of having information about him included in the transfer.
- We recognize, however, that some types of financial information are more sensitive than others.
- This proposal would require consumers to give affirmative consent (**opt in**) before a payment service provider could share a detailed description of personal spending habits with anyone -- medical records held by an insurance affiliate, for example, or information about who we write our checks to or who writes them to us.
- Just as we don't expect a postal worker to read our mail, we don't expect a bank processing our checks to take our most sensitive financial information and then sell a highly personal description of our personal spending habits to outsiders for marketing.

Questions about Proposal Details: Opt-in for Medical Information

Question 16: How does the financial privacy proposal protect medical records within financial holding companies?

- The proposal features strong protections for the privacy of medical records within financial holding companies:
  - First, for companies that are covered by the proposed medical privacy protections under the Health Insurance Portability and Accountability Act, the entire range of strict medical privacy provisions will apply.
  - Second, for life insurance, auto insurance, and other companies that are not covered by the proposed medical rules, the new proposal would require affirmative (opt in) consent before any health information goes from the company to an affiliate or outside company.
  - Third, the proposal contains a new provision that would prevent companies inside financial holding companies from gaining any advantage, in sharing medical information, from their placement in the holding company. The new provision would only allow sharing of medical information, even with the opt-in, if the same information is required of all customers, including those who do not have any other relationship with the holding company. In this way, financial institutions would not gain any extra ability to share medical information when the medical information is held by their corporate affiliates.

<u>Questions about Proposal Details: Opt-in for Medical Information:</u>

Question 17: The sharing of medical records within holding companies was a contentious issue last year during consideration of the financial modernization bill. The Administration opposed the medical privacy provisions in last year's bill and they were dropped at your insistence? What has changed?

- Last year, the Administration was seriously concerned that the proposal on medical records would actually ***lower*** medical privacy protections in major ways. The President's proposal, in sharp contrast, would assure that the strict medical privacy rules would have their full effect.

    - In addition, the President's proposal adds important new protections for medical information within financial holding companies. ***Even for companies that are outside of the scope of the proposed HHS rules, such as life and auto insurance companies***, medical information could be shared with other companies only with affirmative (opt in) consent, and companies would not gain any advantage in sharing medical information by being part of a financial holding company.

<u>Questions about Proposal Details: Opt-in for Medical Information:</u>

Question 18: Does this proposal mean that there is no longer any need for medical privacy legislation?

- Not at all. Because of gaps in HHS's legislative authority, the Administration also strongly believes that we need to enact comprehensive medical privacy legislation to supplement the protections of the HHS regulation.

- The President promised in the State of the Union this year that the proposed medical privacy rules would become final this year. At the announcement of the proposed medical rules, the President stated that they "represent an unprecedented step toward putting Americans back in control of their own medical records." The President also, however, called for passage of a comprehensive medical privacy law. He pointed out, for example, that "only through legislation can we cover all paper records and all employers."

- The proposal today would address the specific issue of limiting flows of personal medical information within financial holding companies. Additional legislation is needed to make sure that proper protections are in place for other uses of medical information.

Questions About Proposal Details: Joint Marketing and Other Exceptions

Question 19: You say you are closing loopholes? Which exceptions have you eliminated?

- ***First, we will close the joint marketing exception.*** Under last year's legislation, financial institutions can share customer information with other companies acting on their behalf or engaged in joint marketing arrangements with them. Consumers have no control over these transfers of information about them.

- This specific "joint marketing" exception was to avoid disadvantaging smaller banks that contract out many services including marketing because they are not part of financial conglomerates and cannot, therefore, rely on affiliate services.

- ***Second, we will level the playing field between affiliates and nonaffiliates.*** Therefore, there is no need for a special exception, particularly one that was not in fact narrowly targeted but undermined consumers' ability to prevent unwanted marketing.

- ***Third, we would eliminate special carve-outs for certain industries.*** Under this proposal, all financial firms will be treated equally.

Questions about Proposal Details: Enforcement

Question 20: How would this bill improve enforcement of financial privacy protections?

- ***Clarify what are violations:*** The proposal would clarify the nature of violations by making clear that it is a violation of law for an institution to fail to live up to the privacy policy disclosures that it makes to consumers.

- ***A second set of eyes (State AGs):*** The bill provides authority for States Attorneys General to enforce the privacy provisions with respect to institutions that are engaged in financial activities, but are not covered by a bank or other financial regulator. These institutions currently come under the jurisdiction of the FTC, which has enforcement powers different from those of financial regulators, and does not have similar examination authority. States will now be able to coordinate with the FTC to improve enforcement for these companies.

- ***Enhanced Penalties:*** The bill authorizes the FTC to seek monetary penalties. Under current law, penalties can only be sought by the FTC for a second violation.

- ***State AG Enforcement of Pretext Calling:*** The bill gives the States AGs similar additional authority to help enforce anti-pretext calling provisions that aim to deter identity theft.

- ***FTC Rulemaking for Certain Entities:*** It would give the FTC the same rule making authority under the Fair Credit Reporting Act as to firms not covered by bank, insurance, or securities regulators as those regulators obtained under last year's legislation for those types of firms.

Questions About Proposal Details: Redisclosure and Reuse

Question 21: What effect would this proposal have on the ability of authorized recipients of information to reuse the information for their own purposes?

- Last year's legislation allows third parties that receive information from a financial institution to transfer the information to others for permitted purposes. However, they can reuse the information, including to do their own marketing, without limits.

- This proposal would tighten the limits on a third party's ability to pass customer information along to another firm and extend the limits to apply to affiliates. It would also limit an affiliate's or third party's ability to reuse information it receives about a customer for its own marketing purposes.

Questions About Proposal Details: Preemption

Question 22: How would this proposal preempt or otherwise affect state law?

- The bill would not make any change in the preemption of state law.

- The inclusion of affiliate opt-out, of course, would apply as a new nationwide floor for consumer protection, as would the other protections included in the bill.

Comparison to Other Bills

Question 23: How does the Clinton-Gore financial privacy proposal differ from the other major privacy bills before the Congress?

- Two other significant financial privacy bills have been introduced, one led by Senators Sarbanes and Leahy, the other by Representative Markey and Senators Shelby and Bryan. (Senator Shelby also has introduced another targeted bill.)

- All are excellent efforts to provide leadership in this important area. While we differ on some details, we applaud the leadership of these members.

The Sarbanes/Leahy bill (S. 187)provides for ***opt-out*** choice for sharing of information among ***affiliated firms***, and ***opt in*** choice for sharing with ***third parties***. Our bill also provides an opt out for all affiliate sharing. However, we offer an opt in for the sharing of the most sensitive information on an individual's spending habits regardless of whether the sharing is with an affiliate or a third party. This provides stronger protections for this information than S. 187. The Clinton-Gore initiative also places an opt in restriction on the transfer of sensitive medical information among financial affiliates, again providing stronger protection. In addition, the Clinton-Gore plan also includes provisions -- not found in the Sarbanes bill -- that strengthen enforcement; address gaps in the protections in last year's financial modernization bill, such as the joint marketing exception; and cover a broader range of institutions and types of financial information.

The Markey/Shelby legislation (H.R. 3320), like the Clinton-Gore initiative and unlike the Sarbanes bill, builds on the protections in last year's financial modernization law. The central difference is that the Markey bill requires opt in consent for sharing with both affiliates and third parties. This approach could have the unfortunate effect of denying consumers too many of the benefits of information sharing, as few customers might make the effort to opt-in even when they have not objection to the nature of sharing of certain less sensitive information. The Clinton-Gore approach focuses the higher opt-in standard on the most sensitive forms of information, namely medical and detailed personal spending data. In other areas, the Clinton-Gore package addresses issues not fully covered by the Markey bill, such as placing stronger restrictions on the reuse of information by those who receive it from financial institutions, and ensuring that consumers can "shop around" for the best privacy protections.

The Shelby targeted legislation (S. __): Shelby's bill, labeled the "Freedom from Behavioral Profiling Act of 2000," would require opt-in for sharing detailed information where you spend money and for what and where you earn money. Despite its name, it does not appear to cover descriptions of spending habits, as the Administration bill does, but that may be a technical drafting issue.

54-0?

THE WHITE HOUSE

WASHINGTON

May 5, 2000

MEMORANDUM FOR THE PRESIDENT

Copied
Sperling
Wartell
Podesta

CC: **JOHN PODESTA**

FROM: **GENE B. SPERLING**
SARAH ROSEN WARTELL

RE: **BANKRUPTCY LEGISLATION**

ISSUE PRESENTED:

The NEC Bankruptcy Working Group has prepared a letter to the Congress setting forth our detailed views on the House and Senate bankruptcy reform bills. Both of these bills passed by overwhelming margins, despite our threat to veto the House bill and the important reservations we expressed about the Senate bill. Consumer groups continue to oppose these bills. Many major editorial pages have been critical of both bills, although most are more favorable toward the Senate bill. We expect some will oppose the final product. The letter to Congress would reiterate our previous statements: It again threatens to veto the House bill and says that the Senate bill better meets your principles, although we have some serious concerns. Despite the lengthy criticism of the bills' provisions, the letter effectively signals that you are likely to sign the final legislation unless it contains the most noxious House provisions or drops most of the consumer and debtor protections achieved by Senate Democrats. We seek your reaction to this strategy before the letter is sent.

VIEWS OF YOUR ADVISORS:

All of your advisors support balanced bankruptcy reform. All believe that the final bill will do some good by encouraging personal responsibility and lowering credit card interest rates that are inflated because some debtors are too ready to use and even abuse Chapter 7's bankruptcy discharge. All of your advisors also agree that, due to an expensive lobbying effort by the credit card industry, the final bill will lack the balance we sought and will not demand similar responsibility from the credit card industry.

An important issue is whether or not the new rules, determining who should be required to go into Chapter 13 (which requires repayment of what a formula says you can repay), are flexible enough to deal with specific cases of hardship in unusual circumstances. The provisions we have pushed for – ultimately allowing the bankruptcy trustees and courts greater discretion – have been largely rejected. We have made reasonable progress in the bill in other areas; for example, the bill protects child support and alimony from competition from credit card debt in many cases and includes a safe harbor from the means test for below-median-income debtors.

Assuming that the final bill that comes to your desk is close to the Senate bill, all of your advisors agree that you should sign it, although for somewhat different reasons. Jack Lew, Chuck Brain, and Gene Sperling believe that, while the final bill may be on the whole a net minus, it is a relatively close call, and not worth the political downside of a veto override. Larry Summers believes that a final bill relatively close to the Senate bill is a net plus and should be signed on the merits. Bankruptcy reform, Larry argues, will have an impact similar to that of open trade: a few visible cases of hardship, but a larger less visible benefit of lower interest rates for credit card borrowers.

All of us feel that, while it is unfortunate that we do not have a more balanced bill, if the final bill stays relatively close to the Senate bill, it would be better to sign the bill with some reservations than to risk a veto override. For you to have any chance of sustaining a veto, or even to make a strong public statement through an override, we would need to launch a high profile battle against a "paid-for" bankruptcy bill – a battle that would indirectly put us at odds with friends like Senators Daschle and Torricelli, and allow others to say we were walking away from our individual responsibility message.

BACKGROUND:

Last May, the House bill passed by a veto-proof margin of 313 to 108. A Democratic substitute that we crafted with Congressman Nadler received only 149 votes and had no effect on our effort to give enough Democrats cover to help us achieve a veto-sustaining margin. Key House Democratic leaders, including Representatives Martin Frost, Bob Menendez, and Patrick Kennedy supported the underlying bill and opposed the Nadler substitute. Minority Leader Gephardt opposed the bill, although he announced his position well after other Members' positions in support had settled. When we talked to Senate Democrats, we found few were interested in our substantive concerns and many were eager to see a reform bill enacted. Some were willing to press for changes and modest improvements were achieved as a result. But few Senate Democrats were willing to oppose the legislation despite its imbalances. As a result, an improved but flawed bill passed the Senate by a vote of 83-14. Democrats opposing the bill on bankruptcy grounds were Senators Kennedy, Wellstone, Dodd, Feingold, Harkin, Reed, Sarbanes, Schumer, Lautenberg, and Moynihan. (A few of the 14 opposed the bill for other reasons.)

Although a formal conference committee has not been named, Congress is now working to reconcile the House and Senate bills. Republican and Democratic leadership expect to attach the bankruptcy provisions to a conference report on other legislation (perhaps Digital Signatures or Crop Insurance) in order to avoid procedural roadblocks placed by Senators Wellstone and Kennedy in trying to force another Senate vote on a two-year minimum wage increase.

The NEC working group drafted a letter to the informal conferees setting forth the Administration's detailed views on various provisions of both bills. It reiterates your senior advisors' veto threat that we issued on the House version of the legislation last May.
It describes the Senate bill as more balanced and doing a better job of meeting your principles, although it details serious concerns we have about some of the Senate bill's provisions.

In a few cases, the letter explains that the House language is actually better than the Senate approach. (The letter also reiterates the veto threat on a bill including the minimum wage, tax, and school voucher amendments that were attached to the bill by the Senate, but we expect those non-relevant provisions to be dropped.) (Copy of cover letter at Appendix A.)

Your senior advisors believe that the relatively muted tone of this letter signals that you are likely to sign the final legislation, albeit with reservations. The details in the letter provide helpful guidance to the Democratic negotiators attempting to improve the bill in conference. Unless we significantly raise the level of our rhetoric now, your advisors will likely recommend that you sign the final bill, unless it drops the most visible improvement achieved by Senate Democrats or includes the most noxious aspects of the House bill.

Appendix B is a more detailed summary of some of our substantive concerns with the House and Senate Bills.

DECISION:

Proceed with Letter ✓ __________ ***Let's Discuss*** __________

APPENDIX A

[Date]

The Honorable Orrin G. Hatch
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Hatch:

The Administration understands that, although conferees have not yet been named, your staff are discussing ways to reconcile the House and Senate versions of H.R. 833, the Bankruptcy Reform Act. The attachment to this letter outlines the Administration's views on these two versions of the bill. As you and your staff develop an agreement on this bill, your consideration of these views would be appreciated.

The President supports balanced consumer bankruptcy reform that would encourage responsibility and reduce abuses of the bankruptcy system on the part of debtors and creditors alike. To meet the test of balance, the bill that emerges from conference should be consistent with the key principles set forth by the President, as described in the enclosure. The President was disappointed that the House once again failed to produce balanced bankruptcy legislation that he could support. As we stated when H.R. 833 came to the House floor last spring, the President's senior advisors would recommend that he veto the House bill if it were presented to him. The bankruptcy provisions of the Senate bill generally do a better job of meeting the President's principles, although the Administration has serious concerns about some provisions.

The Administration notes that certain non-relevant amendments have been included in the Senate version of the bill. The President has made clear on a number of occasions that he strongly supports an increase in the minimum wage of $1 over the next two years. However, as the Administration has stated previously, if Congress sends him a bill delaying the increase, repealing overtime protections for certain workers, adding costly and unnecessary tax cuts that threaten fiscal discipline and direct benefits away from working families, thwarting ongoing efforts to enforce pension law, and including an objectionable private school voucher provision, he will veto it.

Thank you for your consideration of the Administration's views on these bills. We would be happy to discuss any of these concerns with you or your staff.

Sincerely,

Jacob J. Lew

Enclosure

Identical letters sent to The Honorable Patrick J. Leahy,
The Honorable Henry J. Hyde, and The Honorable John Conyers, Jr.

APPENDIX B

SUBSTANTIVE CONCERNS WITH THE HOUSE AND SENATE BILLS

Homestead Exemption: The Senate bill includes a $100,000 cap on the amount of home equity that states can allow debtors to shield from their creditors. The House bill has a cap of $250,000, but allows a state to opt-out, effectively eviscerating the cap. We have argued that it is fundamentally unfair to ask moderate-income debtors to repay what they can, while wealthy debtors can shield their resources in expensive homes. Most expect that the Senate cap will be dropped in conference, although rhetoric on this issue has the greatest potential to embarrass bill proponents.

Credit Card Protections: Although the provisions in both bills are weak, the Senate is somewhat stronger, providing new disclosures on teaser rates and the impact of making only the minimum payment on the length of time one will be repaying debt. Senate Democrats, including the leading Democratic bill proponent Senator Torrecelli, say they will oppose a conference report that further weakens these provisions, so the Senate provisions are likely to survive intact.

Means Test for Chapter 7 Discharge: Both bills use IRS tax collection guidelines to establish tests to determine whether a debtor has the capacity to repay a portion of their debt under a Chapter 13 repayment plan. If so, filing for a Chapter 7 discharge is deemed abuse. The House test is very rigid; the Senate bill has a bit more flexibility. We have argued unsuccessfully that various changes are needed to build more discretion into the system to determine whether, in the debtor's individual circumstances, they really have the capacity to repay (like the IRS has when it used the guidelines for tax collection). We also sought less stringent thresholds and various technical changes to prevent unfairness in the application of the test. Some provisions from each bill are better, but neither bill would address our fundamental concern. We expect a compromise with some of the better and worse features of each.

Protection of Child Support and Alimony: In the last Congress, the First Lady wrote of her concern with provisions that made additional credit card debt nondischargeable in bankruptcy, thus leaving it to compete with higher societal priorities that also are nondischargeable – especially payment of child support and alimony. In response, the bill's proponents added numerous provisions to clarify that child support and alimony are the highest priority. We believe that these provisions will work in many cases to improve the payment of child support and alimony in bankruptcy; however, in a small portion of cases after bankruptcy discharge, where there is no court supervision of child support and alimony payments or wage garnishment, these credit card debts could crowd out child support or alimony. Our argument is very technical; rhetorically, they have neutralized our criticism.

Debtor Protections Against Coercion: During bankruptcy, too many debtors are misled or tricked into agreeing to repay debts that they cannot afford and have a legal right to discharge. The Senate bill contains provisions that make it significantly more difficult to mislead or deceive debtors who cannot afford to reaffirm their debts, although the provisions could be significantly improved to strengthen the hand of debtors seeking remedies when the bill's requirements are not observed. (Certain consumer groups actually oppose the stronger Senate provisions, even though they would prevent many more abusive reaffirmations, because they also may provide creditors with new legal arguments in defending litigation.)

5-9-00

The House bill has far weaker provisions and, most notably, a ban on class actions when seeking remedy for abuse of these requirements. We expect the class action ban to be dropped and the Senate provisions to be retained largely intact, but without the desired improvements. If the class action ban is retained, newfound opposition to the bill may arise.

Clinic Violence: Recently, anti-abortion protesters have used personal bankruptcy to avoid penalties for violence against family planning clinics, some even strategically sending protestors who are judgment proof. Senator Schumer offered an amendment in the Senate that would make court-ordered and other debts resulting from such violence nondischargeable. We strongly supported the amendment. The Vice President was present in the Senate Chamber when they voted on the amendment to break a tie, if needed. To avoid embarrassment, Republicans urged their members to vote for the amendment and it passed by a vote of 80-17. The House has no comparable provision. In conference, they are expected to modify the amendment so that it covers debts from acts of violence generally, so they can avoid special protection for clinic violence debts. There may be technical flaws in their drafting of the broader amendment, so it will not protect all clinic-related debts. Abortion rights groups are not sure whether they want to fix these flaws, preferring to have the issue. If the Republicans drop the provision, Senate Democrats will likely rally; but if they simply broaden it to cover other violence, those eager to vote for the bill will likely concur.

Pension Benefit Protections: The Senate bill also included a provision that would allow debtors to waive in advance bankruptcy protections for certain retirement assets (IRAs and non-ERISA plans). Senator Grassley had earlier offered a provision that would have capped the pension assets that debtors could shield from creditors in bankruptcy, but facing labor opposition to that he instead opted for this. We fear that those of limited means and sophistication could be compelled (perhaps in the boilerplate of a credit card or loan application) to waive protections for the retirement assets. As awareness of this provision has grown, it has provoked a firestorm. We expect it to be modified or eliminated.

THE WHITE HOUSE

WASHINGTON

June 22, 2000

MEMORANDUM TO THE PRESIDENT

FROM: GENE B. SPERLING/SARAH ROSEN WARTELL
CHARLES BRAIN/JOEL WIGINTON

SUBJECT: DECISION ON BANKRUPTCY REFORM LEGISLATION

CC: JOHN PODESTA

ISSUE PRESENTED:

Senator Lott has advised Senator Daschle that negotiations on bankruptcy reform legislation are over. The Republicans agreed to make some further concessions on a couple of the outstanding issues, but the final resolution fails to address our concerns on three key issues you noted in your recent letter to the Congressional leadership: the homestead exemption, discharge of penalties for violations of clinic access laws, and an exemption from the Fair Debt Collection Practices Act (FDCPA) for check collectors. These problems come on top of the dissatisfaction many of your advisors feel with the balance struck in the bill's other provisions. Senator Daschle has asked about your intentions and believes that a strong, clear message from you quickly could enhance the chances of obtaining a veto-sustaining margin.

Your advisors unanimously recommend that you send another letter to the Congress that: (1) indicates that you will veto the bill that Lott described as final; (2) strongly implies that you will sign no bill without adequate clinic access provisions; (3) stresses your concerns with the current resolution of the check collector and homestead issues and the lack of balance in the remainder of the bill; but (4) urges the Congress to fix these problems and leaves you room to decide how to proceed if the clinic access issue is resolved.

STATUS IN CONGRESS

Senator Daschle believes that the chances of achieving 34 Democratic votes are enhanced by your sending a clear, strong veto message as soon as possible. However, it is not certain that a veto-sustaining margin can be obtained. While Daschle would personally support the bill in its current form, if you have a strong veto message premised upon the clinic access and check collector provisions, Daschle may stand with you. Nonetheless, there is some risk, as we have never heard a credible assertion that even 25 Democrats are willing to oppose the bill.

Senator Torricelli, the lead Democratic sponsor of the legislation, also appears to be inclined to support the bill in its current form. Torricelli's staff, however, notes that if you come out with a clear and strong veto statement, the Senator may stand with you against the clinic access and check collector provisions.

Eleven Democratic Senators were opposed to the bill on relevant grounds when it passed the Senate. Senator Durbin, who led the bipartisan effort last year and voted for the Senate bill, has determined that the final bill is unacceptable to him, regardless of the outcome of these remaining issues. Senator Leahy, who voted for the Senate bill and has worked hard to ensure a fair process, believes that the clinic access and the check collector issue swing the balance against an already flawed product; he will vote against it in this form and recommend a veto. Senator Schumer, who strongly opposes the bill, believes that the clinic access issue will mobilize others.

There are five to seven Democrats, led by Senators Biden, Johnson, Breaux, and Reid of Nevada, however, who will likely support the bill in whatever form it is presented to them. Senator Jeffords is the only Republican who has publicly noted some concerns with the measure.

There is little prospect for overcoming the strong veto-proof margin of 313 to 108 by which the House passed its bill last May. Moreover, it is likely that the Republicans will send whatever vehicle they use for the bankruptcy bill to the House first to try to gather momentum.

ADMINISTRATION APPROACH TO BANKRUPTCY REFORM

We have said repeatedly that you support balanced consumer bankruptcy legislation that would encourage responsibility and reduce abuses of the bankruptcy system on the part of debtors and creditors alike. We can eliminate abuse without hurting those forced to turn to bankruptcy, the vast majority of whom are faced with some of the hardest circumstances that life has to offer – divorce, unemployment, illness, and uninsured medical expenses. Although we should not countenance people using bankruptcy to escape bills they can afford to repay, we also should not enact punitive legislation that places insurmountable barriers before the people who file for bankruptcy as a last resort.

To guide Congress in striking the proper balance, we have set forth principles that should be met by a final bill. Many of these issues were resolved on a bipartisan basis by Congressional staff. Others were reserved as "member issues." Just this week, Lott advised Daschle of the Republicans' final offer on these issues and their plan to move forward attaching bankruptcy to the next available vehicle.

ASSESSMENT OF NON-MEMBER ISSUES

In a letter to the informal conferees on May 12, 2000, Jack Lew set forth your key principles. A detailed assessment of the resolution of these issues is in the attached appendix.

In short, the final bill's provisions are closer to the Senate bill than the House bill, but they do not incorporate the balance that you have sought. They reflect a compromise between a House bill that we thought badly one-sided and a better Senate bill about which we still had significant concerns. While all of your advisors believed when we wrote you on May 5th that you should sign a bill close to the Senate bill, this bill is a somewhat closer call.

For example, our fundamental concern about the rigidity of the means test in the Senate bill was not addressed. Moreover, changes were made from the Senate bill to shift a few more debtors out of Chapter 7 and limit a bit further the court's discretion to determine whether a debtor has the capacity to repay. Similarly, flawed language from the Senate bill narrowly limiting the family household goods that debtors can protect from creditor seizure was included in the final bill. While no one of these provisions alone merits your veto, cumulatively they represent undesirable changes relative to the Senate bill.

ASSESSMENT OF RESOLUTION OF MEMBER ISSUES

You wrote to Congressional leaders on June 9th setting out your concerns about five open member issues. Our assessment of the resolution of these issues is below. In short, we believe two of those issues have been resolved to our satisfaction (pension cap and credit card disclosures, although Senator Kennedy is having trouble getting confirmation of the agreement on pension cap); one issue has been resolved to the satisfaction of key Senate Democrats but not to ours (homestead); and the Republican resolution of two issues (clinic access and check collector exemption) is unacceptable to us and the lead Democrats on those issues, although some Democrats would support the bill nonetheless.

<u>Pensions:</u> "The final bill may eliminate protections for reasonable retirement pensions that reflect years of contributions by workers and their employers."

The Senate bill included a noxious provision that would have allowed creditors to demand that debtors waive bankruptcy protection for pension assets as a condition of receiving credit. That was dropped in Conference, but Senator Grassley insisted on some limit on otherwise unlimited pension assets shielded from creditors. Senator Kennedy was deeply concerned that such a cap would send the wrong message about retirement savings. Moreover, seemingly large retirement accounts do not necessarily provide for extravagant lifestyles for workers with increasingly long life expectancies. A compromise was apparently reached between Kennedy and Grassley that caps only certain IRAs, excluding amounts rolled over from employer pension plans, at $1 million. Moreover, the court has discretion to waive the cap in the interests of justice. Senator Kennedy is having difficulty getting confirmation that the Republicans will stick with this agreement. ***If there is no backsliding, this resolution seems reasonable and consistent with our arguments in the homestead context.***

<u>Credit Card Disclosures:</u> "The final bill may weaken important credit card disclosure provisions that will help ensure consumers understand the implications of the debt they are incurring."

The Senate bill requires modest new credit card disclosures. Consumers would be given better information about credit card "teaser rates" and the impact of making only the minimum payment on the length of time one would be repaying debt. Your letter referred to an effort by Senator Gramm to exclude small banks from the provisions' scope. However, the provisions survived without the exclusion, although for two years the Federal Reserve Board will be asked to provide consumers with an 800 number for information about credit cards issued by smaller banks – an 800 number that larger banks will have to provide themselves. ***The Senate bill's modest disclosure requirements have been effectively preserved.***

<u>Homestead:</u> "The final bill may not adequately address the problem of wealthy debtors who use overly broad homestead exemptions to shield assets from their creditors."

State law allows debtors to exempt from the bankruptcy estate home equity valued up to specified homestead exemption thresholds. Five states (including Texas and Florida) have unlimited homestead exemptions, effectively allowing wealthy debtors to shield millions in assets in valuable mansions, while avoid repayment of their creditors. It seems to us fundamentally unfair to ask low- and moderate-income debtors to devote future income to repay all the debts that they can, while leaving loopholes that allow the wealthy to shield assets from their creditors.

The final bill has a modest limitation on unlimited homesteads to address abuse by those who move to states with unlimited homestead exemptions within two years of the bankruptcy filing. ***This does not address our fundamental issue.*** Moreover, wealthy debtors often can use bankruptcy planning to postpone bankruptcy for two years while they qualify for the unlimited homestead exemption.

Senator Kohl, the Democratic Senate champion of this issue, is satisfied that this resolution represents a good first step and establishes the principle that some nationwide limitation on homestead exemptions is appropriate. (Kohl is undecided whether he will support or oppose the overall bill.) Senator Leahy does not want to flank Senator Kohl on the left on this issue. Thus, if you take this issue to the public, you will have only long-time bankruptcy-bill opponents like Wellstone, Kennedy, and Nadler joining you from Congress. However, many editorial pages around the country have pressed this issue hard and would applaud your concern.

Fair Debt Collection Practices Act: "The final bill may include an anti-consumer provision eliminating existing law protections against inappropriate collection practices when collecting from people who bounce a check."

In conference, Senator Hatch has insisted on an anti-consumer provision (in neither the House or the Senate bill) which would eliminate attorneys fee awards for violations of the Fair Debt Collection Practices Act, if the defendant is collecting bounced checks rather than other defaulted debt. This is a pernicious provision because it could give check collectors de facto rein to intimidate and harass lower-income debtors, knowing that their financial position would prevent them from hiring counsel. Often, the only effective enforcement of the check collector provisions is class action litigation, financed by firms because of the potential for attorneys fee awards. Senator Torricelli suggested a minor change, which the Republicans accepted, that limits attorneys' fees to cases where the debtor can prove that he or she had no intent to defraud. Senators Leahy and Sarbanes argue that such a standard is impossible to prove. ***Our fundamental concerns have not been addressed.***

Clinic Access: "Some in Congress still object to a reasonable provision that would end demonstrated abuse of the bankruptcy system. We cannot tolerate abusive bankruptcy filings to avoid the legal consequences of violence, vandalism, and harassment used to deny access to legal health services."

The Senate bill included a Schumer amendment to address the announced strategy of anti-abortion protestors using bankruptcy to avoid penalties for violence against family planning clinics in violation of the Freedom of Access to Clinic Entrances Act (FACE) and its state counterparts. We strongly supported the amendment. The Vice President was in the Senate chamber when they voted to break a tie, if needed. To avoid embarrassment, the Republicans ensured that the amendment passed by a vote of 80-17. However, in conference, they have steadfastly refused to include it or a comparable measure. Their alternative, which they have unilaterally announced will be in the final bill, does little beyond current law. It precludes discharge of all judgements for acts of violence where behavior was shown to be willful and malicious. Advocacy groups argue that few of the actual judgements against, or settlements reached with, defendants who harassed clinic patients include a finding of willful and malicious behavior. Moreover, harassment and intimidation does not always include violence. ***Thus, the final unilateral resolution does not satisfy our concerns.***

This is the hardest issue for the Democrats who want to support the bill. Abortion rights groups are energized. If you take a strong position, this is the issue most likely to rally Democrats in opposition to the bill. Even Senator Torricelli may join you in opposing the bill if further changes are not made to this provision, although Senator Biden does not believe this issue should bring down the entire bill.

RECOMMENDATION

Your advisors unanimously recommend that you send another letter indicating that the Republicans' "final" bankruptcy bill is one that you would veto. The letter would note that there has been an acceptable resolution on pensions and credit card disclosures, but that you have continuing concerns about the check collector, homestead, and clinic access provisions. Special emphasis will be given to the clinic access issue, so that no one reading the letter would doubt you would veto any bill without its satisfactory resolution. A reader should also be concerned that you might veto a bill that does not resolve the homestead and check collection issues to your satisfaction, but the letter will give urge the Congress to fix these problems and give you sufficient latitude to make the veto decision later. There is a real risk that Congress could resolve the clinic access issue, leaving you with only a handful of Democratic Senators joining you in opposition to a bill with the other provisions.

DECISION

____ **1. Send the letter as proposed**

____ **2. Let's discuss**

APPENDIX
ASSESSMENT OF BANKRUPTCY BILL'S OTHER PROVISIONS

In a letter to the informal conferees on May 12, 2000, Jack Lew set forth your key principles. Our assessment of the resolution of these issues is below.

Means Test: "Access to Chapter 7 should not be governed by an arbitrary means test, but by reasonable guidelines that take into account individual circumstances."

We have argued unsuccessfully that various changes are needed to build more discretion into the system to determine whether, in the debtor's individual circumstances, they really have the capacity to repay. We have also sought less stringent thresholds and various technical changes to prevent unfairness in the application of the test. We did succeed in preventing creditors from filing motions to challenge low-income debtors' bankruptcy filings, but these below-median income debtors will be subject to the burdens of new means test paperwork and trustee scrutiny even though only a tiny fraction will have any capacity to repay their debts. While some modest improvements were made in conference, ***the final bill (like both House and Senate bills) does not address many of our fundamental concerns.***

Protection Against Coercive Reaffirmations and Practices: "There must be appropriate safeguards against coercive creditor practices that compel debtors to forgo their rights and that disadvantage more scrupulous creditors."

During bankruptcy, too many debtors are misled or deceived into agreeing to repay debts that they cannot afford and have a legal right to discharge. The final bill contains provisions, based on an Administration proposal, that make it significantly more difficult to mislead or deceive debtors who cannot afford to reaffirm their debts. To get our proposal included in the Senate, we had to make some significant compromises with the credit card industry that cause consumer advocates concern. We sought further improvements in conference but they were not made. However, truly offensive provisions from the House bill (that would have banned class actions as a remedy for existing law violations) were dropped. As a whole, your staff believe ***these provisions are a net improvement for consumers over current law.***

Improving Credit Card Practices: "Both debtors and creditors must be required to be responsible. Bankruptcy reform should be balanced by including provisions that address credit-card practices that may lead to bankruptcies."

As discussed in the body of the memorandum, modest new credit card disclosure requirements were included in the Senate. These largely survived in tact in the final bill. Consumers are given better information about credit card "teaser rates" and the impact of making only the minimum payment on the length of time one would be repaying debt. ***Overall, while we believe more information could be provided more clearly, these provisions are an improvement over current law.***

Non-dischargeable Debts and "Cram Downs": "The goal of repaying creditors must be balanced with the need to protect social priorities, such as payment of child support, alimony, and taxes, and to preserve a meaningful opportunity for a fresh start."

In the last Congress, the First Lady wrote of her concern with provisions that make additional credit card debt nondischargeable in bankruptcy, thus leaving it to compete with higher societal priorities that also are nondischargeable – especially payment of child support and alimony.

In response, the bill's proponents left the new categories of nondischargeable credit card debt, albeit somewhat narrower, but added provisions to clarify that child support and alimony are the highest priority. These provisions will work in many cases to improve the payment of child support and alimony in bankruptcy; however, in a small portion of cases after bankruptcy discharge, these new nondischargeable credit card debts could crowd out child support or alimony. Our argument is very technical, however. ***Rhetorically, they have neutralized our child support and alimony criticism.***

We have a similar concern about provisions in the final bill that would give secured creditors unprecedented rights to collect amounts in excess of the value of their collateral. (Current laws "crams down" their claim to the value of the security. Thus, if a car is worth less than the amount originally borrowed, the claim is limited to the car's value.) Since secured debt must be satisfied if the collateral is to be kept, collection of other societal priorities (like child support, alimony, and taxes) might also suffer a bit. The bill also skews the distribution of scarce debtor assets toward undersecured creditors instead of unsecured creditors (like credit card companies). The latter firms support is ironic, but this was a political bargain they made with car financing firms to win Senator Abraham's support. While the final bill is better than the House provisions, ***our fundamental concern was not addressed.***

Barriers to Entry or Representation in the Bankruptcy System: "Inappropriate barriers should not be created to entry into or effective representation in the bankruptcy system."

The Administration has been concerned about inflexible pre-bankruptcy filing hurdles, including paperwork and counseling requirements and fees. We were also concerned about attestation requirements and sanction provisions that could deter attorneys from representing debtors or raise the costs of representation. The final bill waives fees for low-income debtors, reduces some of the paperwork requirements, and eliminates the most chilling requirements for debtors' attorneys. ***While hardly the provisions we would have written, we do not have strong objections to the remaining provisions.***