BANK POLICY INSTITUTE

April 1, 2019

Via Electronic Mail

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street, S.W.
Suite 3E-218
Washington, D.C. 20219

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: Management Interlocks Act Regulations[1]

Ladies and Gentlemen:

The Bank Policy Institute ("BPI")[2] appreciates the opportunity to comment on the proposal issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal

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1 Thresholds Increase for the Major Assets Prohibition of the Depository Institution Management Interlocks Rules (FRB Docket No. R-1641 and RIN 7100-AF 31; Docket ID OCC-2018-0011 and RIN 1557-AE22; FDIC RIN 3064-AE57) (the "proposal").

2 The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

Deposit Insurance Corporation regarding the agencies' proposed changes to the thresholds for the major assets prohibition of the agencies' regulations implementing the Depository Institution Management Interlocks Act (DIMIA).[3]

We applaud the federal banking agencies' decision not only to increase the thresholds for the major assets prohibition to reflect actual competitive conditions, but also to consider alternative approaches to increasing the thresholds that would account for market changes or inflation. In addition to BPI's support for the immediate increase of the thresholds, this letter describes two additional recommendations for amending the regulations to further the goal of the major assets prohibition to reduce anti-competitive concerns between large depository institutions without unduly limiting the pool of qualified management officials. Specifically, the regulations should index future adjustments to the thresholds to asset growth, and explicitly exempt officials at foreign affiliates and at certain U.S. non-depository affiliates of depository institutions from the interlocks prohibitions.

As noted in the preamble to the 1979 proposal to implement DIMIA, "the purpose of the Act is to foster competition among depository institutions, depository institution holding companies, and their affiliates."[4] We believe the recommendations described in greater detail below are in keeping with the purpose of DIMIA and will not increase anti-competitive risk in the banking industry.

I. The increase in the proposed thresholds to $10 billion is appropriate.

This proposed increase in the major assets thresholds is a welcome change that will have a positive impact in the banking sector. The current major assets thresholds of $1.5 billion and $2.5 billion have been in place since DIMIA was amended in 1996. Since that time, the banking industry has changed so substantially as to make these thresholds out of touch with competitive reality. The agencies' regulations now encompass far too many banking organizations that realistically cannot be considered to have major assets, and thereby reduce the pool of talented management officials. As the proposal notes, the $2.5 billion threshold in 1996 encompassed only 1.3 percent of banking organizations by asset size. At the end of 2017, the $2.5 billion threshold encompassed 4.44 percent of banking organizations by asset size.[5] While banks with assets larger than the stated thresholds are able to request exemptions to the prohibitions against interlocks, the outcome of those requests are unpredictable and have varied over time. Moreover, the lengthy processing periods often delay the ability of the banks to appoint management and directors to open positions and may cause the banks to lose candidates who are unable or unwilling to assume the risk of such delay.

Although the proposal includes three alternatives for increasing the major assets thresholds based on either market changes or inflation, BPI recommends the agencies finalize the proposed increase in the thresholds to $10 billion each. While the proposed alternatives are consistent with the provision in DIMIA that permits the regulatory agencies to adjust the thresholds in order to allow for inflation or market changes, BPI believes that the $10 billion thresholds are more reflective of today's banking industry and, as discussed in the proposal, more accurately reflect the asset size at which interlocks between two depository organizations in different communities may cause anti-competitive harm. As the agencies perceptively noted in the proposal, the $10 billion threshold is also consistent with thresholds used by Congress and the agencies to distinguish between small institutions and larger institutions. With this proposed change, a greater number of depository organizations will more readily be able to fill management and director positions with qualified candidates without needing to request exemptive relief from the agencies.

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[3] 84 Fed. Reg. 604 (Jan 31, 2019).

[4] 44 Fed. Reg. 6421, 6421 (Feb. 1, 1979).

[5] 84 Fed. Reg. at 607.

II. Future adjustments to the asset thresholds should be indexed to asset growth of depository organizations.

Section 204 of DIMIA provides that the "appropriate Federal depository institutions regulatory agencies may, by regulation, adjust, as necessary, the amount of total assets required for depository institutions or depository holding companies" in order to allow for inflation or market changes.[6] Under the proposal, the agencies would continue to make further adjustments to the thresholds to account for inflation through direct final rule without notice and comment. The proposal notes that if the agencies determine that further adjustments to the thresholds are warranted for reasons other than inflation, the agencies would propose other adjustments through notice and comment. BPI supports the agencies' commitment to make periodic adjustments to the asset thresholds. However, BPI believes the agencies should implement the proposal's alternative approach using actual asset growth of depository organizations rather than inflation in order to make future adjustments to the thresholds. As noted in the proposal, the asset thresholds are intended to reflect the size of large institutions in today's market.[7] Using inflation as a measure for determining changes to the asset thresholds may not accurately reflect the size of large institutions as the banking market evolves. To that end, future adjustments to the asset thresholds should be indexed to the asset growth of depository institutions in order to preserve the relationship between the thresholds and the size of the banking industry. BPI further recommends that the agencies make annual adjustments to the major asset thresholds through direct final rule without notice and comment. However, the thresholds should not be reduced below the proposed $10 billion asset amount.

In order to maintain transparency into the changes in the thresholds, BPI recommends that the agencies utilize the asset data that is released on the Federal Reserve's H.8 Assets and Liabilities of Commercial Banks in the United States Statistical Release.[8] BPI recommends that, similar to the alternative described in the proposal, the agencies multiply the thresholds by the annual percent change in commercial bank assets reflected in the H.8. statistical release.

The agencies should also implement grandfather provisions for those instances where the adjustments result in a reduction in the thresholds. When DIMIA was enacted, a person whose service as a management official of two or more depository organizations began prior to the date of enactment was permitted to continue in that service for a period of 10 years from the date of enactment. The agencies included a similar provision in the implementing regulations.[9] BPI recommends that a person whose service in a position as a management official began prior to a reduction in the major asset threshold that causes the service to become prohibited should be permitted to continue in that position for a period of 10 years, beginning on the date the new threshold becomes effective.[10]

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6 12 U.S.C. § 3203.

7 84 Fed. Reg. at 606.

8 Federal Reserve, Statistical Release H.8 - Assets and Liabilities of Commercial Banks in the United States, available at https://www.federalreserve.gov/releases/h8/ (providing weekly aggregate balance sheet for a representative sample of commercial banks). While the H.8 does not provide information on depository holding companies, this report is a close proxy for the changes in assets of depository organizations.

9 See 45 Fed. Reg. 24384, 24391 (Apr. 9, 1980).

10 In the alternative, the agencies could provide a period of two years, with three one-year extensions.

III. The agencies should expand exemptions from the definition of "management official."

The agencies' regulations implementing DIMIA provide that an agency may exempt by agency order an interlock from the prohibitions if it finds that the interlock would not "result in a monopoly or substantial lessening of competition and would not present safety and soundness concerns."[11] In addition, section 208 of DIMIA provides that the agencies may prescribe regulations that "permit service by a management official that would otherwise be prohibited…if such service would not result in a monopoly or substantial lessening of competition…"[12] The agencies have taken advantage of this provision to implement the statutory objectives and have so far included three regulatory exemptions to the definition of "management official." The regulations provide that a management official does not include the following: (i) a person whose management functions relate exclusively to the business of retail merchandising or manufacturing; (ii) a person whose management functions relate principally to a foreign commercial bank's business outside the United States; and (iii) a person described in section 202(4) of DIMIA.[13]

A. *Officials at additional non-depository affiliates should be exempt from the definition of "management official."*

Under the current regulations, management officials at the majority of non-depository affiliates of a depository institution are prohibited from serving as a management official at unaffiliated depository institutions or their affiliates. In granting the exemption for officials whose functions relate to the business of retail merchandising or manufacturing, the agencies noted that the action was in response to commenters' assertion that the term "management official" might be construed to include managers of non-depository affiliates "even though the affiliate does not in fact compete with any nonaffiliated depository organization" and noted that this was not the intended result of DIMIA.[14] The agencies also noted that this exemption applies to a "category of persons whose responsibilities are unrelated to the business of a deposit-taking institution."[15] In granting an exemption to the provisions of the Act, the General Counsel of the Federal Reserve Board has stated that "[t]he general purpose of the Interlocks Act is to promote competition among depository institutions, specifically with respect to the provision of deposit and credit services..."[16] In addition, the agencies, in various rulemakings to implement provisions of the DIMIA, have indicated that the interlocks prohibitions are not intended to apply to all non-depository organizations under the theory not all that these companies in fact compete with any unaffiliated depository organization. In both the 1979 final and the 1995 proposed rules, the agencies requested comment on whether a broader category of management officials at non-depository affiliates should be exempted from the definition of "management official."[17]

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11 12 CFR 26.6(a); 12 CFR 212.6(a) and 238.96(a) (Board); and 12 CFR 348.6(a) (FDIC).

12 12 U.S.C. § 3207.

13 12 CFR 26.2(j)(2) (OCC); 12 CFR 212.2(j)(2) and 238.92(j)(2) (Board); and 12 CFR 348.6(a) (FDIC).

14 44 Fed. Reg. 42152, 42154 (July 19, 1979).

15 60 Fed. Reg. 67424, 64726 (Dec. 29, 1995).

16 Letter, dated July 1, 1997 to Mr. John W. McPartland, from J. Virgil Mattingly, General Counsel of the Board.

17 *See* 44 Fed. Reg. at 6422 (Feb. 1, 1979) (request for comment on the application of the Act to non-depository affiliates of depository institutions in circumstances where such affiliates do not in fact compete with any nonaffiliated depository institution) and 60 Fed. Reg. at 67426 (request for comment on whether the agencies should exempt a broader category of management officials whose duties are unrelated to the provision of financial services by a deposit-taking institution or depository holding company).

The agencies should expand the exemption from the definition of management official to include management officials at non-depository affiliates that do not compete with an unaffiliated depository organization. These companies could include those that neither provide deposit or credit services, nor engage in activities that have been deemed to be so closely related to banking as to be a proper incident to banking under section 4(c)(8) of the Bank Holding Company Act.[18] Companies that do not engage in these activities cannot reasonably be viewed as a competitor of an unaffiliated depository institution as a result of the lack of similarity and substitutability of products and services offered by each. As a result, these interlocks should be permitted as they will not have the anti-competitive effect that the statute sought to prevent.

B. *Officials at foreign affiliates should be exempt from the definition of "management official."*

The current regulations prohibit management officials at foreign affiliates of U.S. depository institutions from serving as a management official of an unaffiliated depository institution or any of its affiliates, which as discussed below, is inconsistent with the goals of the DIMIA. In implementing DIMIA, the agencies made several statements to indicate the focus of the interlocks prohibitions is on the U.S. market and ensure that competition is preserved domestically. The agencies noted that in order to not prohibit interlocking relationships between foreign banks having subsidiary banks or branches or agencies located in the United States, as well as certain interlocking relationships between a foreign bank and a domestic bank, they have "defined the terms 'depository holding company,' 'depository institution,' and 'office'…with reference to location in the United States."[19] The agencies also clarified that the U.S. operations of foreign banks would be subject to the interlocks prohibitions. For example, interlocking relationships between a U.S. branch of a foreign bank and a domestic depository institution or between two U.S. branches of unaffiliated foreign banks would be prohibited under the regulations.[20] The current regulatory framework further clarifies its domestic focus in addressing the treatment of officials at foreign entities by exempting management officials of foreign commercial banks whose functions principally relate to the bank's business outside the United States.

The exemption from the definition of management official should be expanded similarly to include management officials at foreign affiliates of U.S. depository institutions rather than only management officials of foreign banks. The business of foreign affiliates is conducted in the host jurisdictions and as such does not have a nexus to the U.S. banking market and thus is not in competition with the operations of depository institutions or their affiliates in the United States. For example, a U.S. depository organization may have a nonbank affiliate located in Germany. As currently implemented, the management officials of that German affiliate would be prohibited from serving as a management official of an unaffiliated German company with a U.S. depository organization affiliate even though neither of those companies competes with the operations of unaffiliated depository organizations in the United States. As has been stated by the agencies in various proposals, this is not the intended result of the statute.

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[18] 12 U.S.C. § 1843(c)(8).

[19] 44 Fed. Reg. at 42153.

[20] 44 Fed. Reg. at 42154.

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Bank Policy Institute appreciates the opportunity to comment on the proposal. If you have any questions, please contact the undersigned by phone at 202.589.2409 or by email at john.court*@bpi.com.*

Respectfully submitted,

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