Testimony

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TS-027 - Seidman's Oral Statement Before the Committee on Banking and Financial Services on Recent Proposed Mergers of Large Financial Institutions

Office of Thrift Supervision

Remarks, Speeches, & Testimony

Remarks by
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before the
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It is an honor and a privilege to be here today to address your annual meeting. You are among the true pioneers of the community development movement, setting an excellent example of how to invest in underserved communities and do it profitably. The techniques you have developed have leveraged available funding and diversified risk, expanding affordable housing opportunities for both lenders and families.

You have demonstrated the advantages of partnership among financial institutions, federal, state and local governments and other non-profit and community groups. And you have put together projects with many different sources and layers of financing, grants, tax credits and other resources involving disparate interests working together in a spirit of collaboration to making affordable housing a reality. I commend you for your dedication and success.

Like many others, you are asking yourselves "What's next?" To say we live in dynamic times in the financial services business is an understatement. We've talked about modernization, globalization, consolidation and homogenization of banking and commerce for years, but now it's a lot more than talk. It is all happening.

Since 1993, 345 thrifts and more than 1,800 banks have been acquired or merged. Some of the largest mergers have involved California institutions. And it continues, with ever-larger transactions. Washington Mutual and Home Federal; Citicorp and Travelers; Household and Beneficial; BankAmerica and NationsBank; Banc One and First Chicago. One can only wonder what will come next, and there will be a next.

The size and scope of these deals raises important questions about pending financial modernization legislation; about service to the customer, whether individuals, businesses, communities or nations; about regulation and supervision; and about how we continue to solve the credit, community development, and housing needs of this nation.

As most of you know, OTS is directly involved in several of these mergers. Our involvement with WAMU and Home is obvious, but Citicorp, Travelers, BankAmerica, Household and Beneficial also operate federally chartered thrifts. Because of the way the deals are structured, not all of the transactions require our approval, but we are certainly an interested party. How the mergers will ultimately affect the thrifts, we don't know. For the present, the respective managements tell us they expect to continue their thrift operations.

The new Citigroup, combining Citicorp and Travelers, is probably the most interesting of the mergers. It is not only the biggest, but it is also the first to challenge Glass-Steagall and Bank Holding Company Act restrictions by mixing banking, a very large securities operation, and insurance underwriting (not to mention a commodities business) in a bank holding company structure. We understand that under a transition provision of the Bank Holding Company Act, if the Fed approves the transaction, the new entity would be able to continue all of its present operations for two years. The Fed could extend that annually for three additional years. Within that time frame, both companies say they expect that Congress will have enacted financial modernization legislation. And last week, the companies reiterated their desire that Congress attempt to resolve the impasse in enacting meaningful financial modernization legislation this year.

While I'm not betting on the "this year" part of the timetable, the two companies have certainly impressed on Congress the point that, with or without Congressional action, financial modernization is taking form. Ironically, even as we witness financial modernization unfolding in the marketplace - as we all knew it would - Congress' ability to shape it remains as elusive today as it did three weeks ago when HR 10 was pulled from the House floor. And, as members return from recess, we are starting to hear from those whose take on Citigroup and the other megamergers is concern not only about Congress being left behind, but also the possibility that communities and individuals - particularly those now underserved - may come up short.

Clearly, there is resistance to simply reviving HR 10 in its present form, and as I've said before, I think that resistance is appropriate. HR 10 has serious flaws.

While the bill as written would break down barriers to allowing insurance companies and brokerage firms to own banks, it would impose restrictions on the types of activities national banks and their subsidiaries could engage in, including reductions in the extent to which national banks (and therefore state banks operating under wild card statutes) could sell insurance and securities products. Insurance companies and brokerage firms endorsed the measure, but most bankers - particularly community bankers - and thrifts, as well as community and consumer groups, did not.

This reduction in what banks and their subsidiaries can do would also undermine CRA. This would occur in several ways.

- First, of course, to the extent activities are carried out in a bank (or thrift, for that matter), the activity is clearly and directly part of the CRA equation. So if activities are pushed out of the bank, they are less directly subject to CRA.
- Second, activities that take place in a bank subsidiary (but not an affiliate) are automatically part of the CRA "assessment context" which, for the CRA-non-cognoscenti, means in effect they're added in to determine an institution's potential for

engaging in CRA activities. So if activities are pushed into bank holding company subsidiaries, rather than bank subsidiaries, the bank is in effect "smaller" in CRA terms.

- Third, HR10's "push-out" and "non-bank-sub" provisions would simply make the national bank charter less attractive. It's already more expensive for a bank to be regulated by the OCC - to whom they must pay assessments - than by the combination of a state and the FDIC or the Fed, where the FDIC and Fed charge no assessments and the states charge less than the OCC, in part because they share exam responsibility with the two federal agencies. And with wild card statutes and coordinated state exams, other traditional comparative benefits of the national bank charter are being lost.

Now, one might ask, what about thrifts? Interestingly, thrifts and their holding companies operate under a somewhat different paradigm. In return for their extremely limited commercial lending powers, federal savings associations have broader branching rights than national banks, and operate under a somewhat more expansive regime with respect to preemption of state laws that have an impact on core deposit and lending functions. Moreover, because thrifts have never had an exemption from the Securities Acts' definitions of a broker or dealer, securities activities have not been carried out in the thrift itself, but are done generally through a thrift subsidiary instead. The result, given that HR 10 as it emerged from the House Rules Committee pretty much left intact the thrift charter, including the special opportunities of unitary thrift holding companies, is that the CRA concerns of HR 10 with respect to banks do not apply to thrifts.

We are getting closer to modernization after 20 years of debate, but HR 10 as currently drafted is not the right answer. We need legislation that provides more choices for financial services, at competitive prices. We must reach the un-banked and the under-served, and maintain incentives to participate in community development. We want to promote innovation - the creation of new products and new ways to deliver them. And we need to allow businesses choice on how they structure to serve their customers.

The thrift charter answers many of these challenges, with the functional capabilities and affiliations that appear to be those desired in a modern financial institution, for companies that have primarily a consumer, rather than a commercial, focus. There are adequate safeguards built in that limit, for example, upstreaming dividends from the thrift to the parent and transactions with affiliates.

What does the changing financial services industry mean for SAMCO and for community development and affordable housing more generally? It means new challenges and opportunities; the need to adjust, invent and innovate; and an ever-greater need to work in partnership with everyone with a stake in our communities.

Look at your own organization. You started in 1969 with a few thrifts as members. Many of the original members are gone by way of consolidation. But by keeping your membership fee low, you have enabled smaller institutions to join. I understand you have gained more new members in the past three months than in the past three years, many in ethnic markets. That's certainly good news. And the small bank and small thrift are by no means out of the picture. Many of the existing institutions are thriving because they are close to their communities and provide the kind of personal service people and businesses want. And each merger brings groups of former bank and thrift executives into our regional offices applying for new "plain vanilla" thrift charters.

Getting back to SAMCO. You took a dynamic turn when you began financing non-traditional housing projects; and when you developed a structure for tax exempt bond financing. You also opened membership to banks. You have adjusted.

I'm told that although SAMCO has concentrated its support in multi-family housing projects, you are now looking beyond to new types of activities. I applaud you for that. Decent, affordable rental housing will always be needed. But our communities need more: a way for renters to move toward homeownership; continuing education and job opportunities; community services such as health care and day care; better transportation between home and jobs; retail and service establishments; and financial services.

As you develop multi-family housing into the next century, I urge you to consider how your organization can help address the infrastructure needs that accompany housing. Think, for example, about the delivery of services. Is there a way that banks and thrifts can offer alternative banking systems as part of new housing developments? Is there a way to provide day care and health care as part of the development. Are buildings information compliant? Do they allow residents access to technology, such as cable for computers, web TV and the like? Is there access to transportation? Will new housing initiatives further, rather than impede, the ability of individuals to move successfully into the 21st Century? These are critical questions that require thoughtful answers.

Think too, about lending to retail and other small businesses in your communities. They are the backbone of the local economy. Perhaps in conjunction with other lenders and community groups, look into funding the shopping mall that anchors a key corner of the community and is a magnet for new businesses.

Consider how you can impact welfare-to-work programs. Getting employable people off the welfare rolls is one of the keys to a healthy community. Banks, thrifts and organizations like SAMCO, working together, can participate in funding or supporting initiatives, such as microenterprise lending, individual development accounts, job training and/or business development, that help create jobs and prepare people for them. And they can make sure welfare recipients, as well as Social Security recipients and others who receive federal benefits, will have bank accounts they understand and value when electronic benefits transfer kick in next year.

And please don't forget the essential housing counseling programs that have been built up over the past ten years, including post-purchase counseling. If we allow these programs to atrophy because B and C lending is so much easier a way to get houses sold and loans on the books, we will be doing everyone a disservice: the new homeowner saddled with a higher mortgage payment and less understanding of how to meet the challenges of homeownership; the community with vacant, foreclosed homes in its midst; the lender with too much REO; and the hope and optimism that have, over the last five years, lifted the nation's homeownership rate to the highest ever, with huge gains in the number of loans made to minority and low-income families, cut short.

These are matters of keen interest to us at the OTS, which we are addressing through the efforts of our West Region here in San Francisco as well as our other regions. This year, we are expanding our community affairs staff, albeit modestly, and the breadth of our programs. Next Wednesday, the 29th, for example, our Northeast Region is sponsoring a conference in New York on urban home ownership. We'll bring together about 200 representatives of thrifts, other lenders, and community groups to hear about programs that work, the issues involved, such as fair housing, and related subjects.

Then on August 4 and 5, the West Region and our Midwest Region in Dallas are joining forces with the State of New Mexico to sponsor a conference in Albuquerque on lending on tribal lands. Talk about challenge! Solving the credit problems of Native Americans living in tribal communities is one of the most daunting. Hopefully, the conference will help bring attention to the problem and move us along in finding some workable solutions.

In mid-September, our Southeast Region in Atlanta will host a conference on rural economic development. The problems of housing for seasonal, or migrant, workers are unique, and, I might add, about as difficult as any housing problems anywhere. Some of you may be very much aware of the nature of these issues.

These are modest steps, but they are steps on which we hope to build interest that broadens participation and leads to innovative solutions. We're counting on partnerships, such as SAMCO, to help tackle these problems. SAMCO is particularly well positioned, with its experience and understanding of how to bring different sectors of the community together, to deal with such problems. Your leadership sets an example for other partnerships and provides new opportunities for your members to ultimately do things on their own.

And enlist the help of others. I understand that you are considering opening up membership to insurance companies. That's a good start. Our experience with insurance companies, and that of the Neighborhood Reinvestment Corporation, is positive and getting more so every day. Others who are clearly getting interested include utilities, retail businesses, and grocery stores.

We've made much progress over the last twenty years, and over the last five or so, we've gone forward faster than we've gone back, and that's a good thing. We need to celebrate our success, and we need to build on it. SAMCO, together with other dedicated consortia, forms the spine of continued progress in meeting the affordable housing and community development needs of our nation in the years ahead. We look forward to working with you in this critical endeavor.

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