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DEREGULATION OF THE BANKING INDUSTRY
IN THE 1980’s

COLLEEN A. COYNE*

I. INTRODUCTION

The early 1980’s has been a watershed period for banking. Both the market and the competition are changing in dramatic fashion. Enormous changes have occurred in demands for, and means of delivery of, financial services to which banks will have to respond. These market changes have led to intense competition from banking industry outsiders who market appealing products and who are not hampered by banking statutes and regulations which were enacted in the 1920’s and 1930’s to solve problems which no longer are relevant today. In response to these changes, a marked movement toward deregulation of the banking industry has commenced.

Most current banking issues revolve around these recent movements toward deregulation. Specifically, the issues include how state statutes are changing, the need to continue deregulation by modifying the McFadden Act,1 and the removal of restrictions placed on the activities of banks by the Glass-Steagall Act.2

Current regulations which impose restrictions on the banking industry include the McFadden Act, which prohibits interstate bank branching and gives the states exclusive substantive control over intrastate branching by both national and state banks,3 and the Douglas Amendment to the 1956 Bank Holding Company Act, which prevents a bank holding company from acquiring a bank located outside of its home state unless such an acquisition is specifically authorized by law in the state in which the acquisition is sought.4 Also, the Glass-Steagall Act restricts the securities activities of commercial banks and prohibits investment bankers from certain commercial banking activity.5 This Act has effectively separated commercial investment banking up to this point in time.

This article will discuss some of the current issues and events facing the banking industry today and analyze the current status of state laws pertaining to permissible interstate bank activity by bank holding companies. Additionally, the article will indicate how some states are adapting their laws to permit interstate use of automatic teller machines to break through geographic barriers to interstate banking.

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In addition to specific changes in restraints on geographic expansion by banks and bank holding companies, the 1980's have been filled with developments which amount to substantial steps toward the deregulation of interindustry acquisitions of thrift institutions by banks and bank-holding companies. For the first time, in 1982, the Federal Reserve Board granted to the Citicorp bank holding company permission to acquire an out-of-state thrift institution. This shift in regulatory policy was adopted shortly thereafter by Congress when it passed the Garn-St. Germain Depository Institutions Act of 1982.

Another type of deregulation of restraints on interstate banking which has taken place in the early 1980's is the deregulation of "non-bank activities" conducted by banks and bank holding companies. In spite of the Glass-Steagall Act, banks are now being acquired by non-bank organizations, and bank holding companies are commencing brokerage service subsidiaries along with branching into a variety of other non-bank activities.

All of these developments represent some of the changes which are occurring in today's fiercely competitive banking industry. The following discussion will attempt to provide some insight into how these changes are occurring and the impact that each will have upon tomorrow's banking industry.

II. GEOGRAPHIC DEREGULATION

A. Recent State Legislation Under the McFadden Act

State statutes and the McFadden Act of 1927\(^6\) prohibit interstate branch banking, and section 3(d) of the Bank Holding Company Act of 1956 (B.H.C.A.)\(^8\) prohibits interstate bank holding company acquisitions of commercial banks unless such acquisitions are explicitly permitted by the statute of the states. Within the past several years several states have adopted or proposed legislation which explicitly permits acquisitions by out-of-state bank holding companies. However, this form of "nonlocal competition," or banking-related activity in a market by banks headquartered in other cities, appears to be a growing phenomenon in only a subset of financial markets. Generally, these markets all share three characteristics—large size, the existence of specialized submarkets, and growth potential.\(^9\) Characteristically, entry is most common in markets where there is a regulatory advantage to

\(^9\) Heggestad, Non Local Competition for Banking Services, ECON. REV., Aug. 1981 at 21.
operating within the market. The following summarizes the current status of state legislation where regulatory advantage is available to out-of-state financial institutions.

As of September, 1982, five states had passed legislation permitting interstate acquisition of commercial banks by bank holding companies. "Maine is one of three states that allows out-of-state banks to acquire existing banks. Alaska and New York are the other two. Delaware and South Dakota allow only de novo interstate banking on a limited basis." In June, 1975, Maine passed a statute which took effect January 1, 1978, allowing an out-of-state bank holding company to acquire Maine banks if a Maine bank holding company has reciprocal rights in the other state.

In June of 1982, New York amended its banking laws relating to the implementation of section 3(d) of the federal Bank Holding Company Act of 1956 by authorizing the acquisition of control of one or more banking institutions located in New York by an out-of-state bank holding company or subsidiary thereof. The new provision authorizes reciprocal acquisitions. An out-of-state bank holding company may acquire control, directly or indirectly, of one or more New York banks if the laws of the state in which the acquiring bank conducts its business authorizes the acquisition of control of a bank in that state by a bank holding company in New York. The New York statute also permits acquisition of newly organized institutions.

Effective July 1, 1982, Alaska amended its banking laws to permit an out-of-state bank holding company to acquire and own all or any portion of the voting securities or other capital stock of, or all or substantially all the assets of, one or more state banks, domestic bank holding companies, or national banks conducting a banking business in the State of Alaska, unless the state bank or national bank is a recently formed bank (one which commenced banking business in that state on or after July 1, 1982, and that has not been in existence and continuously operating for a period of three years or more). In addition, the out-of-state bank holding company may be required to post bond. The requirements of the Alaska statute are lenient and conducive to more out-of-state bank holding companies taking advantage of this opportunity to expand in that state. Primarily, Alaska does not have the restrictive reciprocity requirement that the New York law has. Therefore, the Alaska law allows a bank holding company from any other state to acquire a state bank, national bank or bank holding company within Alaska.

11 Id.
15 N.Y. Banking Law, § 142-b(3) (McKinney Supp. 1982-83).
16 1982 Alaska Sess. Laws 08.05.255.
17 Id.
According to the Delaware statute, an out-of-state bank holding company or any subsidiary thereof may acquire and hold all, or substantially all, of the voting shares of a single bank located in Delaware, as long as certain conditions are satisfied. The bank whose stock is to be acquired must be a newly established bank that has, or will have when chartered, no more than a single office located in Delaware. Additionally, there is a minimum capitalization requirement on the date of commencement of banking business of $10,000,000 and a minimum of $25,000,000 within one year. The bank may employ no less than 100 persons, and the bank cannot operate in a manner which produces a substantial detriment to existing banking institutions in Delaware. 

South Dakota's statute is similar to that of Delaware. In sections 51-16-40 through 51-16-44, South Dakota permits an out-of-state bank holding company to acquire all, or substantially all, of the shares of a single new bank which is established under the laws of the State of South Dakota and which has a minimum capital stock of $25,000,000, or a single new national bank which is to be located in South Dakota and which has a minimum capital stock of $25,000,000. Acquisitions permitted in section 51-16-40 are limited to a single banking office.

Massachusetts passed an interstate banking law in December of 1982 allowing Massachusetts banks to expand into any other New England state on a reciprocal basis. The bill is sweeping in scope with provisions for mergers, branching, electronic branching and mortgage lending. Maine is currently the only other New England state that allows banking industry reciprocity. Legislatures in most of the other states in the region are expected to consider the issue in 1983.

The Massachusetts reciprocity provision is limited in its application to banks in other New England states enacting reciprocal laws. The regional character of the reciprocity provision is emphasized in the bill which forbids a bank or bank holding company in a state outside New England from acquiring a bank in Massachusetts by first acquiring a bank in another New England state.

In the matter of branching, a Massachusetts bank could establish a "brick and mortar" branch anywhere in New England, if allowed by state and federal laws. National banks would, of course, face the federal branching restrictions of the McFadden Act. Massachusetts-chartered banks would also have legal

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19 Id.
22 Id.
23 Id.
authority to make mortgage loans in any other New England state where that bank has been allowed to establish a "brick and mortar" branch. An exception to the regional approach concerns electronic branches, which the bill allows Massachusetts banks to locate or share anywhere in the nation. Again, however, national banks would face McFadden restrictions.24

An out-of-state financial institution could share with an in-state bank or organization an electronic branch in Massachusetts to allow a customer to make withdrawals, obtain advances against preauthorized lines of credit, and cash checks. The bill allows a financial institution or holding company with its main office in a New England state to "purchase, establish, install, operate, lease, use, or share" an electronic branch in Massachusetts if that state accords similar privileges.25

Several other states have statutes which allow interstate branching on an extremely restrictive basis. "In 1972, Iowa specifically authorized the acquisition of interests in its banks by any out-of-state holding company already owning at least two banks in the state on January 1, 1971. On that date, Northwest Bancorporation was the only out-of-state bank holding company that had two banks in Iowa. The law was held to be constitutional as not violative of 'equal protection.'"26 In July of 1981, Illinois legislators passed a new law revising the Illinois Bank Holding Company Act. The new law permits a bank holding company, registered with the Federal Reserve Board, to acquire an Illinois-based bank provided that the operations of the bank holding company's banking subsidiaries are principally conducted out of the State of Illinois and the bank holding company prior to the effective date of the new law controlled at least two other Illinois-based banks.27 Also, California legislators have been considering a proposal similar to that adopted in Maine.28

Even in states which prohibit interstate banking in any form, banks and bank holding companies are entering into merger agreements with out-of-state financial institutions in the event that bank holding company laws are revised to permit interstate banking. New England banks are leading the nation in making early moves to prepare for anticipated changes in interstate banking regulations currently prohibiting such activity. For example, New England's largest bank, First National Boston Corporation, is taking steps to

24 Id.
28 Shay, supra note 26, at 536.
gain toeholds in neighboring states by acquiring ownership interests in capital-weak banks. Then, when interstate banking barriers fall, it will be positioned to file its acquisition applications. The bank is attempting to minimize any anti-competitive arguments because they are already established in the other states. Under the terms of a present deal, First National also acquired an option to buy an additional twenty percent ownership interest in a Connecticut Bank. The option, however, can only be exercised when state laws permit and with approval of federal regulators.29

Currently, Connecticut law prohibits such a move by an out-of-state financial institution, but it is permitted in Maine, provided that the investor bank is based in a state with similar legislation. Similar transactions, where a major bank holding company has bought preferred non-voting shares which are convertible into common shares when interstate banking is allowed, are taking place between bankers in Oklahoma, Texas, New York, Pennsylvania and Ohio.

B. Automatic Teller Machines

A new technological advancement in the banking industry which is having a definite impact on removal of existing barriers to interstate banking is the development of automatic teller machines (ATMs). In fact, the nation's first coast-to-coast electronic banking transaction, from Washington to New Jersey, using a shared automatic teller machine network, occurred in September of 1982.30

Initially, ATMs were mere cash dispensers. As the technology advanced, off-line units were developed which depended on minicomputers for processing and which used information encoded on the magnetic strips of plastic cards to activate the machines. As consumer acceptance increased and transaction volume expanded, on-line ATMs were developed which have direct access to master or memo files with information on user accounts.

The most common services offered by ATMs include such things as cash withdrawals against checking or savings accounts or against preauthorized credit lines, checking or savings account deposits, payment of installment loans or utility bills, account balance inquiries, and transfer of funds between accounts. Many financial institutions initially installed twenty-four hour ATMs at branch locations to help with peak-hour traffic and to extend banking hours. These off-premises ATMs at strategic locations help to maintain and expand the customer base.31

30 Am. Banker, Oct. 1, 1982, at 1, col. 3.
Although the judiciary has ruled that electronic funds transfer devices are subject to the McFadden Act restraints, use of automatic teller machines by banks across state lines continues to grow. In New Jersey, outright permission has been granted by the state's banking commissioner to interstate use of automatic teller machines. The New Jersey commissioner viewed the arrangement as an extension of the bank in which the machine is located and not as a branch of the depositor's home bank. The ruling sanctioned a link between banks in New Jersey and Pennsylvania that are members of two regional ATM networks. These systems offer depositors of member banks limited privileges across state lines such as withdrawals from accounts, transfers between accounts and obtaining checking account balances. However, customers still are prohibited from making deposits at out-of-state teller machines. The interstate access is available only through cooperative teller networks composed of member banks.

Use of automatic teller machines by banks across state lines is also growing where bank holding companies and banks are acquiring other banks through franchise agreements. A case in point is the acquisition of American Security Bank of Honolulu by the First Interstate Bank Corporation of Los Angeles where, as part of the franchise agreement, the Hawaiian bank will now be linked with a range of services including the Los Angeles bank's automatic teller machine network.

Another innovative use is the installation of ATMs in supermarkets. Publix Super Markets of Florida and Sun Banks of Florida have signed an agreement that will enable Sun Bank customers to make cash withdrawals from the ATM that is placed in the Publix food stores. Sun Banks itself has 161 ATMs, and it also belongs to Cirrus, an ATM network that allows its customers to use ATMs of the other members for cash withdrawals in 35 states. Therefore, visitors to Florida will have access to their cash through ATMs in Sun Banks and in Publix supermarkets. Another progressive ATM coordinator plans to operate automatic teller machines in sixty airports across the country.

Considered a radical innovation less than ten years ago, automated teller machines are now an essential customer service. Not only do they offer increased customer convenience, but they also provide low-cost service. Equally important, a shared ATM network strengthens a bank's ties throughout its geographic region by adding another aspect to its correspond-

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ent-respondent relationships. A shared ATM network is one of the new services regional correspondent banks can offer their respondents. Banks participating in a shared network provide their retail customers dozens, if not hundreds, of locations within their region at which they can conduct routine banking transactions. Moreover, a shared network gives its member banks the opportunity to work with new types of financial institutions. Credit unions, industrial banks, and savings and loan associations can all team up with commercial banks to supply customers increased ATM accessibility.

Satisfying customer demand is just one benefit of a shared ATM network. The network also strengthens the ties between a region's financial institutions in other ways. Clearly, the correspondent bank that helps its customer banks with investments of idle cash, wire transfers, and cash letter processing may develop those relationships even further by selling access to a deposit and withdrawal network. The major regional banks benefit as well. Those banks can expand their geographic marketing area for retail customers, and more importantly for their roles as correspondents within a region, they can also gain access to new financial institutions.

A network may solicit participation from all types of institutions: commercial banks, savings and loan associations, credit unions, industrial banks, consumer finance agencies, and credit card issuers. For correspondent banks, the more successful the product, the easier it is to sell to a respondent and the more it compliments the other services the bank supplies. An ATM network has proven itself to be a service that attracts retail customers. It is successful, and it positively augments the services a correspondent offers.

The services a shared network provides its members and their respondents are keys to the future of banking: to keeping current customers, to attracting additional business, to strengthening regional positions, and to increasing profits. A bank with ATMs throughout the region has a strong competitive edge over banks with weaker regional ties; a bank with strong ties will help its respondents keep up with the state of the art in banking technology. By using electronic fund transfer (EFT) services, which provide convenient, private, and reliable electronic delivery systems, financial institutions are achieving their goal of reducing consumer reliance on "brick and mortar" facilities, paper, and traditional labor-intensive delivery systems. A shared ATM network that operates regionally also positions both major correspondent banks and their respondents to reach additional customers when legislation permits.

III. DEREGULATION OF INTER-INDUSTRY ACQUISITIONS

A. The Citicorp Acquisition

Not only are banking regulators and legislators lifting interstate restrictions, they have also gone so far as to permit cross-industry acquisitions by allowing bank holding companies to acquire thrift institutions.
Even after the Deregulation Act of 1980, thrift institutions in our country were still faced with numerous problems.

For thrift institutions, deregulating interest rates exacerbated liquidity problems. The cost of funds increased dramatically, while low-interest mortgage assets turned over much more slowly. By mid-1981, the number of problem cases among institutions regulated by the FSLIC had climbed to 263, compared with just seventy-nine in late 1979. As federal regulators were quick to point out, these troubled institutions threatened both the deposit insurance system and the stability of the banking industry itself.\(^{37}\)

In an effort to curtail these continuing problems, the Federal Reserve Board and the Federal Savings and Loan Insurance Corporation (F.S.L.I.C.) approved the first cross-industry, cross-country takeover\(^{38}\) which was followed shortly thereafter by congressional legislation providing for just this type of transaction.\(^{39}\)

In October of 1982, the Federal Reserve Board published its order approving the acquisition of Fidelity Federal Savings and Loan Association of San Francisco, San Francisco, California, by Citicorp, New York, New York.\(^{40}\) In light of the emergency nature of the situation at Fidelity and its deteriorating financial condition, the Federal Reserve Board (F.R.B.) acted expeditiously upon the Citicorp acquisition.

Citicorp is a bank holding company within the meaning of the Bank Holding Company Act (B.H.C.A.) of 1956. As of June 30, 1982, it is the second largest banking organization in the United States. Fidelity is a savings and loan association, headquartered in San Francisco, California, primarily engaged in taking savings deposits and making loans to individuals secured by mortgages on real property. Citicorp's banking subsidiaries and Fidelity operate in separate market areas.

The Citicorp acquisition was filed under section 4(c)(8) of the Bank Holding Company Act, which deals with permissible non-banking activities of a bank holding company. The Federal Reserve Board ruled that Fidelity was not a bank under the Act.\(^{41}\) Therefore, the interstate banking prohibition of section 3(d) of the Bank Holding Company Act did not bar the Board's approval of Citicorp's application.\(^{42}\) The Board believed that a federally insured savings and loan association that offers NOW accounts and exercises no greater commercial lending powers than are now permitted to a federal savings and loan association under the Home Owners' Loan Act of 1933 (HOLA),

\(^{38}\) Citicorp, \textit{supra} note 6.
\(^{39}\) Garn-St. Germain, \textit{supra} note 7.
\(^{40}\) Citicorp, \textit{supra} note 6, at 656.
\(^{41}\) \textit{Id.} at 657.
as amended, is not a "bank" for purposes of the Bank Holding Company Act.\textsuperscript{43}
This decision by the Board was based upon the important facts that the lending activity of savings and loans has historically been highly specialized and, under the current statutes and regulations, continues to be concentrated in home mortgage.\textsuperscript{44} A key factor in the Board's decision was the conclusion that because Congress has left intact a separate statutory and regulatory framework for the operation of savings and loans and banks, it was Congress' intent that federally insured savings and loans not be subject to the restrictions of the Bank Holding Company Act.

The Board's analysis of the application included an additional step. Section 4 of the B.H.C.A. generally prohibits a bank holding company from engaging, either directly or indirectly, or through a subsidiary, in nonbanking activities.\textsuperscript{45} The Board had to decide if the transaction between Citicorp and Fidelity fell within the exception to this prohibition contained in section 4(c)(8) of the Act. This exception authorizes a bank holding company to acquire a company engaged in activities that the Board "after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking as to be a proper incident thereto."\textsuperscript{46}

In determining whether an activity is a proper incident to banking, section 4(c)(8) requires that:

[T]he Board shall consider whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices.\textsuperscript{47}

This second step of analysis of Citicorp's application required that a two-part test be answered. First, the Board determined whether the activity is "closely related to banking." Second, it determined whether the performance of the proposed activity by the applicant bank holding company might reasonably be expected to produce public benefits that outweighed the resulting adverse effects. The Board reaffirmed its view, as expressed in American Fletcher Corp.\textsuperscript{48} and other decisions,\textsuperscript{49} that the operation of a savings and loan association is an activity closely related to banking.

Next, the Federal Reserve Board determined the "proper incidents" of


\textsuperscript{44} Citicorp, \textit{supra} note 6, at 661.


\textsuperscript{47} \textit{Id}.

the operation of the savings and loans as an affiliate of the bank holding company. The Board has not been prepared to permit bank holding companies to acquire thrift institutions on a general basis. However, the Board has consistently regarded the B.H.C.A. as authorizing the Board to permit such an acquisition where the public interest might dictate that the Board use its existing authority under the Act to approve inter-industry acquisitions on a case-by-case basis.

In August, 1982, the Federal Home Loan Bank Board (F.H.L.B.B.) had determined that there was no evidence the rate of decline in Fidelity's position would slow or that its condition could improve unless it was acquired by an institution, with greatly superior resources, that could rebuild public confidence in Fidelity. In view of this determination of emergency financial condition at Fidelity by the F.H.L.B.B. (the primary supervisory authority for Fidelity), the substantial savings to the F.S.L.I.C. through the Citicorp proposal, the present circumstances of the thrift industry and the financial condition of a large number of its members, along with increased competition and greater convenience to the public through restoration of Fidelity as an effective competitor and the satisfaction by Citicorp of the credit needs of Fidelity's communities, the Board determined that consummation of the Citicorp proposal could reasonably be expected to result in substantial public benefit. Furthermore, the Board concluded that Citicorp had both the financial and managerial resources necessary to acquire Fidelity and make it a viable competitor without significant effects on Citicorp.

As part of the total analysis of the Citicorp application, the Board carefully examined all possible adverse factors resulting from the acquisition, including the conflict between the statutory and regulatory frameworks within which banks and savings and loans operate, the erosion of institutional rivalry between banks and savings and loans, and the potential for undermining federal interstate banking prohibitions. Other possible adverse effects include the potential for decreased or unfair competition, conflicts of interests, financial risks, diversion of funds, participation in impermissible activities, evasion of interest rate limitations, unsound banking practices, and undue concentration of resources.

In view of Citicorp's limited presence in the relevant California markets served by Fidelity, the number and size of financial organizations operating in these California markets, the legal prohibitions against Citicorp's expa-

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46 Supra note 6, at 657.
47 Id.
48 Id. at 658.
49 Id.
sion of its bank subsidiaries into California, and the fact that Fidelity is a failing institution with limited competitive vigor, the Board concluded that the proposal would not have any significant adverse effects on existing or potential competition in any relevant market. Indeed, the proposed acquisition would have a substantial beneficial impact on competition by ensuring the continued operation of Fidelity as a viable institution through its access to the financial and managerial resources of Citicorp. The Board concluded that consummation of the proposal, subject to the conditions set out in the Order, as described below, may not reasonably be expected to result in conflicts of interests, unsound banking practices, undue concentration of resources, or other adverse effects.

The affiliation of Citicorp and Fidelity also is not likely to result in unfair competition in view of the various conditions imposed by the Board that require Fidelity's independent operation and forbid its use to further or enhance the activities of Citicorp's other subsidiaries. In addition, Fidelity's activities will be limited to those permissible under the Act, and its offices will be limited to locations at which banks located in California may establish branches. To guard against possible adverse effects of affiliation in this case between a banking organization and a savings and loan association, including the potential for unfair competition and diversion of funds, the Board has established the following as conditions for its approval of the application:

1. Citicorp shall operate Fidelity as a federal savings and loan association having as its primary purpose the provision of residential housing credit. .

2. Fidelity shall not establish or operate a remote service unit at any location outside California.

3. Fidelity shall not establish or operate branches at locations not permissible for national or state banks located in California.

4. Fidelity shall be operated as a separate, independent, profit-oriented corporate entity and shall not be operated in tandem with any other subsidiary of Citicorp. Citicorp and Fidelity shall limit their operations to effect this condition, and shall observe the following conditions: (a) No banking or other subsidiary of Citicorp shall link its deposit-taking activities to accounts at Fidelity in a sweeping arrangement or similar arrangement. (b) Neither Citicorp nor any of its subsidiaries shall solicit deposits or loans for Fidelity; nor shall Fidelity, directly or indirectly, solicit deposits or loans for any other subsidiary of Citicorp.

5. To the extent necessary to ensure independent operation of Fidelity and prevent the improper diversion of funds, there shall be no transactions between Fidelity and Citicorp or any of its subsidiaries without the prior approval of the Federal Reserve Bank of New York. This limitation encompasses the transfer, purchase, sale or loan of any assets or liabilities, but does not include infusions of capital from Citicorp or the payment of dividends by Fidelity to Citicorp.
6. Citicorp shall not change Fidelity's name to include the word "bank" or any other term that might confuse the public regarding Fidelity's status as a nonbank thrift institution.

7. Fidelity shall not convert its charter to that of a state savings and loan association or other state chartered thrift institution or to a national or state commercial bank without the Board’s prior approval.\textsuperscript{54}

Approval of this cross-industry, cross-country takeover represents a reversal of a fifty year-old policy of general prohibition against bank acquisition of financial institutions in other states, and it seems to end the recurring regulatory question of whether operation of a savings and loan association is a “proper incident” to commercial banking. The September approval marks the first time the Board has approved a cross-state takeover by a bank holding company.

Proponents of the Citicorp acquisition contend that it will result in increased competition and, therefore, will benefit customers. It is argued that it best serves the customer's interest to bring in a new and viable organization which could be aggressively competing for deposits and loans at rates better than those currently offered.

However, opponents of the interstate acquisition argue that the Federal Reserve Board's decision, in effect, permitted Citicorp to purchase a market-entry exemption into California. Critics contend that this type of decision should be made by Congress and the state legislature, not just the F.H.L.B.B. and F.R.B.\textsuperscript{55} (Their argument lost its force as a result of the 1982 Garn-St. Germain Depository Institutions Amendments whereby Congress did approve such a measure.) Those opposing the Citicorp acquisition view it as another nail in the coffin of legal prohibitions on interstate deposit taking, enabling Citicorp to tap California's rich deposit market without waiting for the eventual legalization of interstate banking. Those resisting the recent move by the Federal Reserve Board see the approval as a major blow against the important American tradition of keeping financial power decentralized. These individuals fear that this is the forerunner of other similar decisions that will concentrate financial power in the hands of a few.\textsuperscript{56} Opponents also would prefer to see interstate banking accomplished on a nationwide basis, as opposed to the piecemeal approach taken by the F.R.B. in the Citicorp decision.

Under existing law, the Citicorp acquisition represents a good way to gain a major retail deposit gathering capability in a very desirable market. This is especially valuable due to the 1982 Act granting savings and loans the same powers that commercial banks have. However, Citicorp paid a high

\textsuperscript{54} Id. at 658-59 (footnotes omitted).


\textsuperscript{56} Am. Banker, Aug. 17, 1982, at 1, col. 2.
price for the acquisition. If the McFadden Act or the Douglas Amendment were to be eliminated in the near future, and bank holding companies were able to enter the highly desirable markets without acquiring local institutions, Citicorp’s acquisition would turn out to be a costly mistake.

B. 1982 Garn-St. Germain Depository Institutions Act

Beginning in 1974, the Federal Reserve Board recommended to Congress that section 3(d) of the Bank Holding Company Act of 1956 be amended to allow approval of large, single, out-of-state acquisitions by bank holding companies in emergency situations involving problem or failing banks. Although the Board’s annual reports to Congress for 1975, 1976 and 1978 renewed its recommendations for amendment, it was not until October of 1982, the same month that the F.R.B. approved the Citicorp acquisition, that Congress took action and passed the Garn-St. Germain Depository Institutions Act.

On October 15, 1982, the President signed the Depository Institutions Act of 1982. The financial reform bill is intended to provide the means to begin restructuring depository institutions, enabling them to compete in the new financial environment. The new law provides a federal assistance program for weak depository institutions, expands thrifts’ powers on commercial and consumer loans, and creates a new instrument to enable depository institutions to compete with money market mutual funds. However, it contains no provisions dealing with the important question of delivery of other financial services, including security activities by banks and other depository institutions. Such regulation is expected to be decided by Congress in 1983.

Specific provisions of the new bill authorize the Federal Deposit Insurance Corporation to grant “Extraordinary Acquisitions” “[w]henever an insured bank with total assets of $500,000,000 or more . . . is closed.” The corporation has discretion to determine and to arrange the sale of assets and the assumption of liabilities by an insured depository institution located in the state where the closed bank was chartered but established by an out-of-state bank or bank holding company. The Federal Deposit Insurance Corporation (F.D.I.C.) is also granted the authority to determine that an insured bank organized in mutual form may be merged with, or its assets purchased by, and its liability assumed by another institution, including an insured depository institution located in the state where the insured bank is chartered but established by an out-of-state bank or bank holding company.

In reference to the Bank Holding Company Act of 1956, 12 U.S.C. section 1842, the 1982 bill further provides that:

57 Shay, supra note 26, at 550.
59 Id.
60 Id. § 116(3)(A)(ii), at 1477.
Notwithstanding Section 3(d) of the Bank Holding Company Act of 1956 or any other provision of law, State or Federal, or the constitution of any state, an institution that merges with or acquires an insured bank under paragraph (2) or (3) is authorized to be and shall be operated as a subsidiary of an out-of-State bank or bank holding company, except that an out-of-State bank may operate the resulting institution as a subsidiary only if such ownership is otherwise specifically authorized.61

Section 116 of the 1982 Act provides certain conditions and requirements before these extraordinary acquisitions will be permitted. The subsidiary shall be subject to the conditions upon which a national bank may establish and operate branches in the state in which such insured institution is located.62 The acquired institution is prohibited from moving its principal office or any branch office if a national bank would be so forbidden.63

The Act prohibits the acquisition if a monopoly would result or if competition is substantially lessened.64 Also, the Act prescribes a priority schedule for the F.D.I.C. to follow when it determines which prospective purchaser or merger partner to authorize the transaction with. The Act provides:

(B) In considering authorizations under this subsection, the Corporation shall give consideration to the need to minimize the cost of financial assistance and to the maintenance of specialized depository institutions. The Corporation shall authorize transactions under this subsection considering the following priorities:

(i) First, between depository institutions of the same type within the same State;

(ii) Second, between depository institutions of the same type in different States;

(iii) Third, between depository institutions of different types in the same State; and

(iv) Fourth, between depository institutions of different types in different States.

(C) In considering offers from different States, the Corporation shall give a priority to offers from adjoining States.65

Congress also provided for “Emergency Thrift Acquisitions,” amending Section 408 of the National Housing Act as follows:

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61 Id. § 116(4)(ii), at 1477.
62 Id. § 116(4)(iii), at 1477.
63 Id. § 116(4)(iii), at 1477.
64 Id. § 116(7)(A) & (B), at 1478.
65 Id. § 116(6)(B) & (C), at 1478.
(m)(1)(A)(i). Notwithstanding any provision of the laws or constitution of any
State or any provision of Federal law, except as provided in subsections (e)(2)
and (1) of this section, and in clause (iii) of this subparagraph, the Corporation,
upon its determination that severe financial conditions exist which threaten
the stability of a significant number of insured institutions, or of insured in-
stitutions possessing significant financial resources, may authorize, in its
discretion and where it determines such authorization would lessen the risk to
the Corporation, an insured institution that is eligible for assistance pursuant
to Section 406(f) of this Act to merge or consolidate with, or to transfer its
assets and liabilities to, any other insured institution or any insured bank (as
such term 'insured bank' is defined in Section 3(h) of the Federal Deposit In-
surance Act), may authorize any other insured institution to acquire control of
said insured institution, or may authorize any company to acquire control of
said insured institution or to acquire the assets or assume the liabilities
thereof. 66

However, the F.D.I.C. must obtain approval from the state official having jur-
sisdiction of the acquired institution.

These emergency thrift acquisitions are subject to some of the same con-
ditions and requirements as prescribed in section 116 of the 1982 Act. The
F.D.I.C. must follow the same priority list when considering prospective pur-
chasers or merger partners as in section 116 of the Act. 67

Analysis of the Committee reports on the Garn-St. Germain Depository
Institutions Act of 1982 reveals that Congress aimed to revitalize the housing
industry by strengthening the financial stability of home mortgage lending
institutions and ensuring the availability of home mortgage loans. 68 The Sen-
ate amendments and the bill granted the federal depository institutions
insurance agencies increased flexibility in order to effectively assist troubled
and financially distressed institutions. The 1982 Act enhanced the ability of
the Federal Deposit Insurance Corporation and the Federal Savings and
Loan Corporation to aid institutions in need of assistance by expanding the
forms of financial assistance that could be provided by the agencies. It pro-
vided specific procedures for the agencies to follow in order to facilitate the
acquisition or merger of failed or failing institutions. It also provided some
guidelines for emergency authorities of the regulatory agencies.

The Act’s provision allowing banks or bank holding companies to acquire
ailing thrift institutions is generally regarded as increasing the opportunities
for inter-industry mergers. However, the legislation may have the opposite
effect. The Federal Reserve already had the authority to approve bank
holding company acquisition of savings and loan associations, but, except for

66 Id. § 123(a), para. (m)(1)(A)(i), at 1483. (Section 408 of the National Housing Act is codified at
12 U.S.C. § 1739(a)).
67 Id. § 123(a), para. (m)(3)(B)(i)- (iv), at 1484.
a few unusual situations, the Federal Reserve has refused to do so. In light of the Federal Reserve's reluctance, it is likely that the F.R.B. will interpret Congress' failure to include a provision on bank holding company operation of "healthy" thrifts as a prohibition against such activity. Still, some view the 1982 Amendments as a back door repeal of the long-standing restrictions on interstate banking by commercial banks continued in the McFadden Act and the Douglas Amendment.

Some members of the banking community view the 1982 Act as an erosion of the statutory bar on interstate banking to the point where the prohibition is virtually meaningless. At the 38th annual meeting of the National Savings and Loan League in Denver on October 12, 1982, Richard T. Pratt, Chairman of the F.H.L.B.B., said that the recent actions by the Depository Institutions Deregulation Committee could result in a large-scale interstate deposit gathering and may increase the mobility of retail funds to a level never before experienced. Pratt was referring to the Depository Institution Amendments of 1982 which allow brokerage of savings deposits and the creation of the new instrument which enables commercial banks and thrifts to compete with money market funds. Pratt warned that if the new account was combined with the rule that associations may employ brokers on any savings account, then an institution with a broker has a nationwide deposit gathering mechanism.

The 1982 Act again raises the question of whether thrifts should be considered competitors of banks when mergers are examined under antitrust laws. The 1982 bill allows federal savings and loan associations to make secured and unsecured commercial, corporate, business or agricultural loans up to five percent of their assets until January 1, 1984, and thereafter up to ten percent of their assets. The federal savings and loan associations are also authorized to take deposits from their customers. Under the Bank Holding Company Act, 12 U.S.C. section 1824(d), these two functions define a "commercial bank." This will certainly add to the growing sentiment that thrifts must be considered part of the commercial banking "line of commerce" when analyzing the effects on competition by banking mergers permitted under the new Act.

Traditionally, the United States Supreme Court has considered banks alone, at the exclusion of thrifts, to be the banking "line of commerce." The Court based its decisions on the fact that the "unique cluster" of bank ser-

68 Id.
69 Garn-St. Germain, supra note 7, § 325, at 1500.
vices provided by commercial banks distinguished itself as a distinct line of commerce separate and apart from thrift institutions. The Court did not find that the products comprising the cluster were all individually economically distinct, but rather that it was the gathering together of such products in one facility—a department store of finance—that was unique. Thus, it has rejected attempts to include thrift institutions in defining the market product.

However, in United States v. Connecticut National Bank, the Court qualified its decision not to include savings and loans in defining the relevant line of commerce, allowing for the possibility that “[a]t some stage in the development of savings banks it will be unrealistic to distinguish them from commercial banks for purposes of the Clayton Act . . . that point may well be reached when and if savings banks become significant participants in the marketing of bank services to commercial enterprises.” Thus, the Court did not foreclose “the possibility that changes in the powers of thrift institutions will eventually warrant their inclusion in the same product market with commercial banks."

Two recent district court cases have reconsidered the role of thrifts as “significant participants” in the commercial banking product market. In neither case did the court include thrifts in defining the relevant product market. In both, however, the presence of thrifts was considered in evaluating the merger's likely impact on competition. A number of commentators have argued cogently that the changes in the marketplace caused by deregulation and competition of unregulated institutions require that the product line be redefined. The distinctions of a bank as a distinct “line of commerce” may be fast eroding. As a result of the changes made in the 1982 Amendments, it may now be practical to consider non-bank financial institutions as

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32 374 U.S. at 356. The Court noted that the relevant “line of commerce” in which to measure the competitive effects of proposed bank mergers is the cluster of products (various kinds of credit) and services (such as checking account and trust administration) denoted by the term commercial banking. Other examples of banking products are listed in 374 U.S. at 326 n.5.

33 While the Supreme Court has consistently held that the appropriate line of commerce included only commercial banks, several district courts have held otherwise. See, e.g., United States v. First National Bancorporation, 329 F. Supp. 1003 (D. Colo. 1971); United States v. Phillipsburg National Bank, 306 F. Supp. 645 (D.N.J. 1969); United States v. First National Bank of Jackson, 301 F. Supp. 1161 (S.D. Miss. 1969); United States v. Crocker-Anglo National Bank, 277 F. Supp. 133 (N.D. Cal. 1967). In these situations the Supreme Court has noted that the district courts have erred in their interpretation of the Court's reasoning on line of commerce.

34 418 U.S. at 666.


37 See Raven, supra note 77, at 406 n.63.
in direct competition with commercial banks and within the same "line of commerce."

Those still opposing the inclusion of thrifts within the commercial bank's "line of commerce," including the United States Department of Justice, the Federal Reserve Board, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation, argue that the thrifts will have the potential to be competitors. They may not have to exercise their new powers to be considered competitors. The F.R.B.'s position is that thrift institutions do not compete actively with commercial banks over a sufficient range of financial services to consider them full competitors. However, the Office of the Comptroller of the Currency (O.C.C.) has acknowledged thrifts' competition in an approval of Hartford National's acquisition of Connecticut National Bank. The O.C.C. said thrift competition should be fully factored into any assessment of a proposed banking merger.79

In sum, the Garn-St. Germain Act is an historic milestone in the deregulation of depository institutions and in the evolution of the thrift industry. Building upon the partial foundation provided by the 1980 Deregulation Act, it culminates some twenty years of financial restructuring efforts. From the thrift industry perspective, it provides the legislative framework for short-run survival and long-run competitive viability. In fact, it creates a single industry out of the heretofore separate savings bank and savings and loan industries.

While the Garn-St. Germain Act has not resolved all of the outstanding issues in financial regulation, it has cleared the deck for action in other important areas. The next Congress will almost surely address the Glass-Steagall separation of the banking and securities businesses, specifically, whether banks should be permitted to underwrite revenue bonds, along with issues concerning geographic restrictions on interstate branching and bank holding company operations.

IV. DEREGULATION OF NON-BANK ACTIVITY BY BANKS AND BANK HOLDING COMPANIES

A. Acquisitions of Banks by Non-Bank Organizations

Today, acquisition-minded corporations and investors are looking for banks, but they do not want the restrictions imposed by the broad range of banking laws. The general viewpoint that is prompting the recent influx of non-bank institutions into the thrift and commercial banking markets is the sense that the country will undergo very profound changes in the delivery systems of consumer financial services. Within all the stresses and strains which exist today, there are opportunities to put together a national, or at least multistate, delivery system.

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As a result of a little-known interpretation of the federal Bank Holding Company Act by the Federal Reserve Board, it has become possible for a consumer finance company, retailer, insurance company, broker-dealer and, for that matter, any other type of company to acquire a bank either by selling the bank's commercial loan portfolio or by not offering checking accounts. A "bank" is defined in the Bank Holding Company Act as an entity which accepts demand deposits and makes commercial loans. By eliminating one of these two functions, an entity is no longer considered a "bank" for purposes of the Bank Holding Company Act. This "loophole" may also make it possible for bank holding companies to acquire banks in several states even though the federal Bank Holding Company Act generally prohibits interstate acquisitions of banks.

Until recently, the conventional wisdom was that consumer finance companies, retailers, insurance companies, and broker-dealers would be precluded from acquiring or organizing banking subsidiaries because of the requirements of the federal Bank Holding Company Act which prohibit "banks" from being affiliated with companies involved in businesses which are not related to banking. During the past two years, however, a few consumer finance companies, including one located in Pennsylvania, and Parker Pen Company have acquired national banks located in California, Delaware and New Hampshire and have avoided registration as bank holding companies under the federal Bank Holding Company Act by requiring the banks that they acquired to divest their commercial loan portfolios.

Because retail businesses, like insurance companies and broker-dealers, are engaged in businesses which are not related to banking, bank holding company registration would have been prohibited by federal law. Future activities of bank holding companies are severely restricted by the Bank Holding Company Act, and most consumer finance companies, retailers, insurance companies, and broker-dealers (even if they were eligible to register as bank holding companies) would not want to be subject to those restrictions.

All of these drawbacks may be avoided by employing the commercial loan divestiture technique, which makes the bank being acquired a non-bank for purposes of the federal Bank Holding Company Act. The acquired bank, nevertheless, has all the characteristics and authority of traditional commercial banks except that it may not offer commercial loans. Alternatively, the bank may continue to offer commercial loans if it ceases to offer checking accounts payable on demand.

Although a company which seeks to acquire a bank by using this "loophole" need not file an application with the Federal Reserve Board under the

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Bank Holding Company Act, the company must file a Notice of Change in Control under the federal Change in Bank Control Act. The notice must be filed with the Comptroller of the Currency (in the case of a national bank), the Federal Deposit Insurance Corporation (in the case of a state-chartered non-member bank), or the Federal Reserve Board (in the case of a state-chartered member bank).

The acquisition may be consummated unless the appropriate agency objects within 60 days after the application is filed. There have been very few instances where an agency has objected. The Change in Bank Control Act, unlike the federal Bank Holding Company Act, does not impose any restrictions with respect to future activities of companies affiliated with the acquired bank.

All of the banks that have been acquired by using this technique have been national banks. This is not surprising in light of a national bank’s clear ability to “export” interest rates from its home state throughout the country, without regard for usury laws in other states. The banks that have been acquired have been located in states which do not have usury ceilings. As a result of provisions in the Depository Institutions Deregulation and Monetary Control Act of 1980, even a state-chartered bank whose deposits are insured by the F.D.I.C. generally would have the right to “export” interest rates throughout the country without regard to state usury laws in effect where the borrowers reside. This latter provision may be very important to securities broker-dealers which desire to acquire banks. Although the federal Glass-Steagall Act prohibits national banks and state-chartered banks that are members of the Federal Reserve System from engaging in the investment banking business either directly or through affiliates, there is no prohibition against a state-chartered non-member bank being affiliated with a broker-dealer provided that such an affiliation is not prohibited by state law.

The major advantages of such an acquisition for a consumer finance company, retailer, insurance company, or broker-dealer are: (a) the ability of a national bank (or even a state-chartered bank) to “export” interest rates throughout the country; (b) diversification into offering a wide variety of loan and credit products (e.g., credit cards, second mortgages, and unsecured loans by mail, checking and NOW overdraft accounts. It would also appear that retailers who have been hampered by restrictive usury laws in their home states may organize or acquire national banks in states, such as Delaware, that have no interest rate limitations and issue credit cards to their customers located in their home states such as Pennsylvania, and charge interest above the rates allowed by their home states); (c) the ability to offer F.D.I.C.-insured deposit products (e.g., money-market certificates, passbook

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accounts, NOW accounts, checking accounts, IRA accounts; (d) the ability to participate in government direct-deposit programs (e.g., Social Security); (e) the ability to establish or participate in an automatic teller machine network or other forms of electronic funds transfers systems; (f) the ability to offer Visa or MasterCard debit cards which may be used nationwide; (g) the ability to engage in interstate banking by acquiring a network of "consumer" banks; and (h) the ability to offer trust services, pension plans, and other such services.84

Even existing bank holding companies may be able to take advantage of this "loophole." Although the Bank Holding Company Act prohibits an out-of-state bank holding company from acquiring a bank in another state without the express legislative consent of the other state, it would appear that a bank holding company located in one state could acquire a "consumer" national bank in another state without that state's express legislative consent as long as the bank has divested its commercial loan portfolio prior to the acquisition and makes exclusively consumer loans after the acquisition. This may also be a relatively easy way for a small or medium-sized bank located in a state that is hampered by that state's usury law to reestablish its consumer lending or credit card operations in a state which has no interest rate limitations and to use that state as a base from which it may "export" interest rates into its home state.

We may have seen just the "tip of the iceberg," and it would not be surprising if within the next year or two a major retailer, insurance company, or broker-dealer uses the divestiture technique in order to enter the banking business. It would also not be surprising if this technique is used by a bank holding company in order to avoid the prohibitions against interstate ownership of banks. Although the Independent Bankers Association of America has strenuously objected to the Federal Reserve Board's recognition of this "loophole" and has suggested to Congress that this loophole be "plugged," it is unlikely that Congress will act on this suggestion, given the trend toward deregulation in the banking industry.85

An example of the current movement to acquire banks by non-bank corporations occurred in December of 1982 when the Federal Deposit Insurance Corporation granted authority for Dreyfus Corporation, a New York based mutual fund, to assume control of a New Jersey commercial bank, in spite of vigorous opposition by the Federal Reserve Board. The controversial approval may even result in the conflict being resolved by the courts.86

The acquisition was achieved by using the loophole in the Bank Holding

85 Id.
Company Act. Larger banking organizations are siding with the F.D.I.C. on the touchy issue of allowing non-banking entities to become their competitors because they view the issue as a means of putting pressure on Congress to take another look in 1983 at the legal definition of a banking organization and its powers. These organizations see the issue as an opportunity to broaden their powers.

The provision of the law used by Dreyfus to acquire the New Jersey bank is receiving increasing attention. A conglomerate, a furniture store, and a pen company are among those which have used the provision to enter the banking field, and other businesses are considering the same move. Lobbyists representing these larger banks believe they have a good chance of broadening 12 U.S.C. section 1843(c)(8) in the 1983 session. With the Treasury already on record in favor of a drastic liberalization of the standard, the existing climate for deregulation is likely to work for them.

Meanwhile, the F.R.B. is very concerned about the idea of mixing banking and other forms of business. Such a mixture has often been blamed for the banking disasters that occurred during the Depression years. The Federal Reserve Board opposes the establishment of a national bank operated by a mutual fund because it violates sections 20 and 32 of the Glass-Steagall Act, which prohibits banks from "engaging directly or indirectly in certain types of securities activities." This position taken by the F.R.B. has put the Board at direct odds with the F.D.I.C.

The Federal Reserve Board has characterized the proposed use of the banks for funding money-fund operations as constituting an "impermissible commingling of banking and commerce and is prohibited by the Bank Holding Company Act." The F.R.B. has determined that the Bank would continue to be a "Bank" under the B.H.C.A. definition by defining a "commercial loan" as any loan other than one where the proceeds are used "to acquire property or services used by the borrower for personal, family, household or charitable purposes."

The moves surrounding Dreyfus' application are being watched closely by bankers and mutual-fund operators. It is widely felt that the company's attempts to gain a banking toehold are an attempt to strengthen its competitive position with banks, which are now competing with the money funds for customers. The F.R.B. is expected to ask Congress to address the issue comprehensively in the 1983 session.

Dreyfus contends that it is simply an investment advisor to no-load mutual funds and is not within the prohibitions of the Glass-Steagall Act. It

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Id.
further argues that its revenues from the distribution of mutual fund shares are so miniscule that it cannot be properly deemed to be primarily engaged in the distribution of securities within the meaning of the Glass-Steagall Act.

With respect to the F.R.B.'s challenge on Bank Holding Company Act grounds, Dreyfus had stated in its application to the Comptroller that the proposed bank would not engage in the business of making commercial loans and therefore would not be a bank within the meaning of the Bank Holding Act. The F.D.I.C.'s position, after reviewing analagous acquisitions of "non-bank banks," is that there are a number of clear precedents, dating back a number of years, for the bank to be held exempt from the B.H.C.A.'s definitions of bank based on its divestiture of its commercial loan portfolio prior to the acquisition and its agreement not to engage in the business of making commercial loans in the future. By failing to object previously to that now fairly routine practice, the Federal Reserve Board has acquiesced in, if not expressly agreed with, a more limited definition of commercial loan on which the public has come to rely.

Heretofore, the Federal Reserve Board's analysis of what constitutes a commercial loan has focused on direct lending activities and has not suggested that the entire spectrum of money market activities and interbank transfers of funds should be incorporated into the concept. The Board's consistent use of a more limited definition of commercial loan led to the warranted assumption that the term included certain activities and excluded others. Now, in its analysis of the Dreyfus acquisition, the Federal Reserve Board has dramatically recast the definition of commercial loan by including within it certain activities that clearly had been excluded from the definition in the past.

While the F.D.I.C. has acknowledged the Board's authority to interpret the B.H.C.A., it believes that such a radical departure from the traditional view of what constitutes a commercial loan raises issues beyond the scope of regulatory interpretation. The F.D.I.C. is in general agreement with the Federal Reserve Board about the desirability between banking and commerce; however, Dreyfus is a financial services company and not a corporation engaged in general commerce. Moreover, the F.D.I.C. feels its would be inappropriate for the F.D.I.C. or the Federal Reserve Board to undertake to resolve these kinds of public policy issues and firmly believes that Congress is the appropriate authority to reassess the statutory distinctions among banking institutions, thrifts, securities firms, and other providers of financial services and to resolve the underlying question of the permissible activities of banks and bank holding companies.

The F.D.I.C. would join the Federal Reserve Board in requesting the Congress to undertake a comprehensive review of this issue. However, it does not support stop-gap or stand-alone legislation to merely redefine the term "bank" or "commercial loan." The far-reaching developments in the market-
place that have occurred over the past decade do not lend themselves to a simple solution along these lines. These developments call not for regulatory re-interpretation, but for legislative action.

In sum, the F.D.I.C. concluded that it was constrained to follow the clear legal precedents established over the years and that any change in policy should be brought about by congressional, not agency, action. It intends to support in 1983 a broad-based congressional review of the activities in which banks, thrifts, and their holding companies of affiliates should be permitted to engage.  

This feud between these two federal banking regulators over the Dreyfus Corporation application to acquire the New Jersey bank has evolved into a debate of what constitutes commercial lending. The F.R.B. argument is that the bank, despite its disclaimer, still would do commercial lending because it is likely to be in the business of issuing bankers' acceptances, bank certificates of deposit, and commercial paper. The F.D.I.C. has countered that these kinds of activities normally are not considered commercial lending functions, and has thus accused the F.R.B. of trying to "dramatically recast" the definition of commercial loan in light of the Dreyfus case. The F.R.B. is likely to face some stiff opposition to its attempt to tighten the definition of the term "bank" from the Treasury Department, the Office of the Comptroller of the Currency, and large bank holding companies.

B. Brokerage Service Subsidiaries

The Garn-St. Germain Depository Institutions Act set up the framework within which bankers can respond to the competitive challenges of their non-bank financial services competitors. Deregulation has flung open the door to competition, creating a mad scramble among the banks for new products, marketing strategies, and market share. An important part of this trend is the entry of banks and thrift institutions into the discount brokerage business.

Tomorrow's financial services industry will include firms of many types and sizes. With the crumbling of regulatory barriers to competition, it is anticipated that on the national scale, the number of full-range competitors is likely to increase. This expansion will probably be followed by a period of contraction and consolidation, as some firms realize that they have insufficient knowledge or the practical experience necessary to compete on such a large level. Most analysts agree that the financial supermarket will co-exist and operate side by side with smaller firms which are able to identify specific needs of consumers and thereafter move quickly to fulfill them. The desire to

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be competitive in tomorrow's environment has already caused a number of firms to position themselves for the future. Acquisitions by securities firms and acquisitions of securities firms by both financial and non-financial institutions underscore the dynamic forces at work in the industry.

Now that the banking industry has achieved greater banking deregulation, banking leaders are now beginning a drive for new legislation which will broaden the list of financial services that commercial banks can provide. Key leaders of the American Bankers Association are recommending endorsement of a 1981 Treasury Bill which would accomplish this goal by drastically expanding the power of bank holding companies. The legislation, with an accompanying Treasury analysis, would seem to allow the bank holding companies to sell virtually any financial service, with the only limits being those imposed by general antitrust statutes or other existing bank laws. Such a proposal is sure to face tough opposition from non-bank competitors, including the insurance, securities, data processing, and real estate industries, causing some friction between the larger and smaller banks. But first impressions suggest that this issue may be less divisive than the bitter battle fought last year over deregulation.\(^1\)

The Treasury legislation would repeal section 4(c)(8) of the 1970 Bank Holding Company Act. The section limits the bank holding companies to acquisitions that are closely related to banking and are in the public interest, and requires the Federal Reserve Board to clear all bank holding company (BHC) acquisitions. Under the Treasury bill, the section 4(c)(8) limitation would be replaced with a far broader list of permissible activities that would be drawn up by the Federal Reserve Board. Also, prior F.R.B. approval of all BHC acquisitions would no longer be required. A Treasury Department statement that accompanied the bill stressed that the F.R.B.'s list of permissible activities should "expand upon" existing BHC powers, noting that the list should include investment advice, extensions of credit, leasing, real estate development and brokerage services, data processing, underwriting and brokerage services for the sale of insurance, and investing in underwriting, or acting as broker for the sale of "investment media." The Treasury stressed that it was not recommending that the BHC services be limited to this list. The treasury bill to be endorsed by the American Banking Association would also allow commercial banks to underwrite and deal in revenue bonds, but only through a separate subsidiary. The larger banking organizations, fueling the drive for expanded powers, want this underwriting authority, but they still consider the revised standard for acquisitions to be the most important part of the legislation.\(^2\)

The commercial bankers' philosophy behind offering a discount broker-

\(^1\) Am. Banker, Jan. 14, 1983, at 1, col. 4.
\(^2\) Id. at 10.
Deregulation of the Banking Industry in the 1980's

BANKING DEREGULATIONS

...age service is to provide a more sophisticated service which allows banks entry to a previously inaccessible market. The new products are viewed not only as a way to maintain the banks' current market share, but also as a vehicle with which to attract new, upscale customers in the future. This view is a common thread among banks entering into linkages with other players in the financial services industry. The decision to offer discount brokerage services is not a hasty, makeshift reaction to competition from powerful non-bank competitors. Rather, it represents a forward-looking attempt by some banks to position themselves for the future, based on a recognition and acceptance of the fundamental changes occurring within the financial services industry.

Some regard banks as being ideally situated to market financial services. They have enormous assets, a presence in the local community, are well-known and trusted, and have credibility. Others, however, do not see financial institutions as the most effective competitors in the changing financial markets. With the competition for consumers of financial services, many believe that the securities industry is better positioned to compete in the world of tomorrow since it already operates in a telephone-based, electronic environment, in sharp contrast to the slower paced, face-to-face deposit or insurance business. It will be easier to build an upscale market through a business customarily transacted over the telephone than one which operates mainly on the basis of personal contact. The transition to the financial environment of the future may very well be less difficult for today's securities industry participants.93

As competition pushes for banks to provide "full service" and federal regulations rapidly change, banks will be offering financial futures and securities activities. In August of 1982 the Comptroller of the Currency approved a bank's plan to establish a subsidiary to operate all facets of the discount brokerage business and to expand its discount brokerage services outside the state to other banks.94 Other bank holding companies are seeking to expand into discount brokerage services after obtaining approval from the Federal Reserve Board.

On January 7, 1983, the Federal Reserve Board allowed BankAmerica Corporation to acquire Charles Schwab & Company, Inc. by ruling that the discount brokerage operation was "closely related to banking."95 Additionally, the F.R.B. approved the acquisition without imposing any conditions on how the securities company could operate.96

In order for the F.R.B. to approve the application, the agency had to rule

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96 Id.
that Schwab's brokerage activities were closely related to banking and that the proposed non-banking activity by a BHC affiliate would reasonably be expected to produce public benefits that outweighed possible adverse effects. The F.R.B. decision stated that Schwab's brokerage services were operationally and functionally similar to the brokerage services that are generally provided by banks, and that banking organizations are particularly well-equipped to provide these types of services. The use of sophisticated techniques, resources, and personnel to execute orders for the purchase or sale of securities for customer accounts is sufficiently widespread in the banking industry to justify a finding that banks are capable of handling retail brokerage services. For these reasons, and because Schwab's margin lending, maintenance of customer securities accounts, and custodial services were similar to banking services, Schwab's activities were considered closely related to banking.

Regarding the public-benefits test, the F.R.B. decided that Schwab's affiliation with BankAmerica, a large, internationally recognized, and diversified banking and financial services company with substantial resources, could reasonably be expected to result in enhanced public recognition and confidence in Schwab in particular and discount brokers in general. Strengthening Schwab as a competitor would likely have a pro-competitive impact on price competition in the retail brokerage industry, and thus outweigh any possible adverse effects that might result from the merger.

In opposition to the brokerage acquisition, the Securities Industry Association (SIA) charged that the proposed acquisition could allow Bank of America NT&SA, BankAmerica's principal banking subsidiary, to use Schwab's services in situations that would result in a breach of fiduciary duty. The SIA also stated that since Schwab is a high-risk enterprise, BankAmerica might be compelled to make unsound loans to shore up the discount brokerage company. Furthermore, because BankAmerica intends to advertise its affiliation with Schwab, the acquisition could result in public confusion. The F.R.B., however found no basis for the SIA's contentions.

In addition to the F.R.B.'s approval of a securities subsidiary by a BHC, the Comptroller of the Currency may soon allow national banks to open operating subsidiaries—including discount brokerage companies—without going through a formal application process. A recently issued proposal would replace the formal application with a notification process. If the rule is adopted, a bank would only be required to notify the Comptroller of its intentions 30

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97 Id.
98 Id.
99 Id.
101 BankAmerica, supra note 94.
days before it established or acquired an operating subsidiary. In addition to
discount brokerage companies, banks would also be able to establish any cor-
poration involved in a banking-related activity, such as check clearing and
data processing. If adopted, the Comptroller's proposal would put national
banks a step ahead—in terms of opening securities subsidiaries—of state
banks and federal savings and loan associations because the regulators of
those institutions maintain requirements for formal applications. A
spokesman for the Comptroller's office said that the agency's plan is intended
to reduce the burden on banks by simplifying the agency's procedures. The
proposal, he added, is part of the agency's overall evaluation of the applica-
tion and review process. Although the F.R.B. recently approved the
BankAmerica Corporation acquisition of Charles Schwab, an official of that
agency said the activity would have to have "more history" before the F.R.B.
considered allowing banks to open securities subsidiaries without going
through a formal application process.\(^{102}\)

The financial services industry of tomorrow—from the securities side—is
starting to take shape. The last act will be played when Congress makes a final
determination concerning the Glass-Steagall Act. In spite of the obvious
benefits large financial conglomerates can produce, their success or failure
will ultimately depend on their ability to render personalized service. The
full-service firm, through its registered representatives, will have to become
more efficient in order to secure its future.

Although the smaller firm is unlikely to have the resources available to it
to market a full line of packaged products and services, indications are that
these products may be obtainable on a wholesale or syndicated basis through
some of the larger firms. Through some form of joint venture or through the
wholesaling of nationally known products by nationally known firms, product
gaps are likely to be filled for even the smallest of firms. Some of the large
firms may soon offer their uniquely designed products bearing their name to
others for sale through the purchasers' distribution systems.

One such alternative being offered by investment companies to out-of-
state banks which are not affiliated with the bank holding company is known
as a "Sweep Account." This account is a specialized service offered to the
bank where the investment firm automatically transfers, or "sweeps," the
balances from a checking or negotiable order of withdrawal account into
higher yielding investments of the customer's choice, including money
market funds.\(^{103}\) The account enables these independent banks to compete
directly with large bank holding companies without having to join them. This
service is attractive to banks because it enables bankers to custom-design
financial programs.

\(^{102}\) Am. Banker, Jan. 21, 1983, at 1, col. 1.
\(^{103}\) Am. Banker, Oct. 6, 1982, at 3, col. 1.
In summary, banks may use several methods to enter the discount brokerage field. They may purchase an existing firm, as Bank of America purchased Schwab. Alternatively, they may contract with brokers to provide execution, clearing, safekeeping, and reporting services for the bank's clients, as scores have already done. Finally, banks can use new financial technology to create a network that ties existing retail services with securities capabilities already available in the banks' trust departments. Whichever way they proceed, the banks have demonstrated their willingness and ability to enter the discount brokerage field.

The recently enacted Depository Institutions Act of 1982, which authorized banks and thrifts to establish money market accounts free of interest rate controls, should take considerable pressure off Congress to amend the Glass-Steagall Act. Generally, Glass-Steagall prohibits banks and other depository institutions from underwriting or dealing in nongovernment securities directly, and in the case of member banks, indirectly through affiliates.

Although the ability to take market-rate deposits, established by the 1982 Act, should silence most of the cries of the smaller banks and thrifts of unfair competition from money market funds, the larger money-center banks are eager to offer the range of financial services now being offered by their non-bank competitors. These services include a full range of cash management service, securities underwriting and dealing, and particularly the highly profitable and low-risk revenue bond underwriting business which have heretofore been forbidden because of Glass-Steagall. A closer look at the Act, however, reveals that the foregoing generality is applicable to member banks only.

Specifically, although Glass-Steagall contains a fairly comprehensive set of prohibitions against member banks engaging directly or indirectly in securities dealing and underwriting, only one provision of the Act, section 21, has universal application to all depository institutions. Section 21 generally prohibits a securities firm engaged in underwriting and dealing from also taking deposits.

Although case law construing Glass-Steagall is sparse, the Supreme Court recently concluded in Board of Governors of the Federal Reserve System v. Investment Company Institute that even though section 21 may prohibit banks (and thrifts) themselves from engaging in certain securities activities, it does not prohibit affiliates from engaging in such activities. The Court's construction of section 21 highlights that while Glass-Steagall restricts member-bank affiliations with securities firms engaged in underwriting and dealing, nonmember banks and thrift institutions, such as savings and loan associations, are not subject to such restrictions on affiliations.

This nonmember-bank "loophole" could become very significant since the benefits of F.R.B. membership are questionable in light of the 1980 legislation that gave nonmember institutions access to the Federal Reserve Board's discount window and other services. Moreover, assuming a nonmember bank engages in securities underwriting and dealing through a subsidiary rather than through a holding company affiliate, the Bank Holding Company Act and its prohibitions against engaging in non-banking activities do not apply, leaving state law as the only possible statutory barrier.

In response to a lawsuit brought by the Investment Company Institute challenging the establishment of a money market fund by the Boston Five Cent Savings Bank, the F.D.I.C. issued a general policy statement on September 1, 1982, regarding the permissible securities activities of nonmember insured banks. The F.D.I.C.'s policy statement is that the Glass-Steagall Act:

does not, by its terms, prohibit an insured nonmember bank from establishing an affiliate relationship with, or organizing or acquiring, a subsidiary corporation that engages in the business of issuing, underwriting, selling, or distributing at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities. While the Glass-Steagall Act was intended to protect banks from certain of the risks inherent in particular securities activities, it does not reach the securities activities of a bona fide subsidiary of an insured nonmember bank.

Thus, while the Supreme Court has confirmed the right of nonmember banks to operate securities affiliates under Glass-Steagall, the Boston Five Cent litigation should shed some light on the question of to what extent interaction can exist between a bank (or thrift institution) and its securities affiliate without running afoul of section 21 on an alter-ego theory. Unfortunately, the question offers no easy answer, as the solutions must necessarily vary from case to case.

Since the Federal Reserve Board has adopted the position that "[a] bank holding company should not engage, directly or indirectly, in the sale or distribution of securities of any investment company for which it acts as investment advisor," the conflict between this position and the F.D.I.C. position leaves little doubt that Glass-Steagall has reemerged as one of the most debated and scrutinized statutes of the day, primarily because of the combination of high interest rates and below-market ceilings on deposits mandated by Regulation Q. As interest rate controls are gradually phased out, as required by the Depository Institutions Deregulation and Monetary Control Act of 1980, and the new money market accounts are introduced, Glass-Steagall will become less of a concern for most depository institutions whose

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primary objective has been to attract market-rate deposits competitive with money market funds.

Larger depository institutions, however, will continue to push for expanded securities powers, including acting as broker-dealers, underwriting revenue bonds, and sponsoring investment funds, in order to compete with the non-bank financial conglomerates. For them, Glass-Steagall will remain very much a target for change. However well the Glass-Steagall Act has served its purpose over the years, it is ill-equipped to deal with the transformation that is taking place in the financial services industry. The Boston Five proposal highlights the unevenness of Glass-Steagall and will hopefully fuel efforts in Congress to review the Act as a whole and, in particular, those provisions which discriminate against member banks.

Although the securities industry is expected to take every step to block further nonmember bank entry into the securities business, if it relies on Glass-Steagall as its defense, the industry's efforts will ultimately fail since Glass-Steagall is quite clear on this issue. If Congress and the policy makers view the continued separation of commercial banking and investment banking as being in the public interest, then Glass-Steagall should be amended to clarify that objective and to regulate all depository institutions equally. Similarly, if bank participation in securities underwriting and dealing through affiliates is deemed appropriate, then Glass-Steagall should be revised to permit all banks and thrift institutions—not just nonmember banks—to engage in such securities activities through affiliates.

C. Other Non-Banking Activity

Banks are continuing to expand their services to include traditional "nonbank services." In addition to banks offering brokerage services to their customers and banks being acquired by non-bank organizations, bank holding companies are acquiring futures commission merchant subsidiaries, bank service corporations, data processing, insurance, trust businesses, industrial banks, and mortgage companies through the operation of subsidiaries.

Major banks are lining up to become brokers of financial futures. Such banking services will yield new revenues by hedging an institution's own portfolio to lessen exposure to market rate risk; by providing large corporations with advice as to hedging programs; and by dealing with the asset/liability imbalance confronting many institutions.

While there has been no congressional repeal or modification of the Glass-Steagall Act, nor is one likely in the near future, federal regulatory agencies are taking actions allowing banks and savings and loans to compete with all financial institutions. Proponents argue that permitting banks to enter the futures and securities markets will enhance competition and improve financial services available to the consumer. On the other hand, oppo-
nents argue that this type of deregulation may encourage the possibility of unsound financial practices by inexperienced commercial banks and that it will result in domination of the securities industry by large commercial banks.

Banking companies must go through two sets of approvals before they can execute orders in the futures markets for their customers. First, they must win the approval of the Comptroller of the Currency or Federal Reserve. Then, they must apply to the Futures Trading Commission for registration as a broker. As of December, 1982, only two banks had completely cleared the regulatory mill. In July of 1982, the Federal Reserve Board, with its authority to regulate subsidiaries of bank holding companies, granted an application to J. P. Morgan, Inc. to operate a futures commission merchant subsidiary. The Federal Reserve Board viewed the futures activity as “incidental to banking” and, therefore, permissible under the Bank Holding Company Act. Also, the Comptroller of the Currency approved the operation of a futures commission merchant subsidiary to North Carolina National Bank. Further, the F.H.L.B.B. now permits savings and loans to participate in the interest rate futures market. Several other brokerage subsidiaries have applications pending approval with the Futures Trading Commission. These developments demonstrate that federal financial regulators are now allowing depository institutions to seize marketing opportunities and to compete effectively with other providers of financial services.

Another recent change in banking regulation which resulted in an expansion of permissible banking services occurred in another section of the 1982 Garn-St. Germain Depository Institutions Act. The Senate amendment allows one or more banks to form a bank service corporation in which they may invest up to ten percent of their unimpaired capital and surplus. No bank may invest more than five percent of its assets in bank service corporations. A service corporation can engage in the same activities as its parent banks and is authorized to perform any activity permissible under the Federal Reserve Board’s Regulation Y (permissible non-banking activities).

Under the Act, “a bank service corporation may perform at any geographic location any service, other than deposit taking, that the Board has determined, by regulation, to be permissible for a bank holding company under section 4(c)(8) of the Bank Holding Company Act.” The 1982 Depository Institutions Amendments could prove to be the “uncut gem” of the financial re-

109 Id.
111 Garn-St. Germain, supra note 7, § 709, at 1540-44.
112 Id. § 709(4)(f), at 1542.
form bill passed by Congress. The new service corporation powers could be a key to the future success of many banks, particularly the smaller ones, giving them a long-term opportunity for expansion and flexibility.

Until October, 1982, bank service corporation activities were limited to data processing, check clearing and similar operational functions. Under the 1982 legislation, one bank or more can form a service corporation that could engage in any activity of a bank as well as any permissible non-bank activity of a bank holding company. The expanded service corporation powers will provide the bank with an opportunity to affiliate themselves and provide services and activities within a bank service corporate structure where a bank holding company structure would be far too ponderous, too difficult, onerous, or expensive. Now a group of small banks in a service corporation will be able to offer a mortgage-servicing operation.

Bank holding companies have also received permission from the Federal Reserve Board to expand services enabling them to engage in data processing services. In July, 1982, the F.R.B. permitted Citicorp to form a subsidiary to offer data processing services. In a second action, in August of 1982, the F.R.B. broadened the Board's Regulation Y, which governs activities of bank holding companies, to permit all such institutions to offer the services. These actions by the Federal Reserve Board have not gone unchallenged. The Association of Data Processing Service Organizations, which represents about 560 computer services companies, filed an appeal in the United States Court of Appeals for the District of Columbia in October of 1982.

The 1982 Depository Institutions Amendments also included a provision which generally prohibits bank holding companies and their subsidiaries from providing insurance, including property and casualty insurance products, as a principal agent or broker with six specific exceptions enumerated in the title. Thus, the amendment establishes that the sale of insurance does not, except for activities subject to the exceptions, meet the "closely related" test of section 4(c)(8) of the Bank Holding Company Act.

Although the 1982 Amendments prohibit banks from engaging in the insurance business, there still exists much support for the position in favor of expansion into the insurance field. New York legislators are seriously considering major changes in insurance regulations allowing carriers to expand into the banking field. Recommendations for reform include increasing banking powers to insurers, but only if these powers are balanced by increased insurance powers to banks. This recommendation is made with respect to the

116 Garn-St. Germain, supra note 7, at § 601.
increasing competition banks are encountering from other non-bank financial intermediaries. Such legislation would revolutionize the investment standards for the insurance industry nationally. The legislation will permit limited trading in interest futures as a hedging tool for investment by life insurance companies.\textsuperscript{117}

Various other events have occurred recently in the banking community, all of which resulted in expansion of banking services and/or out-of-state acquisitions. One such acquisition occurred when the Federal Reserve Board and the Comptroller of the Currency granted authority to commercial lending institutions to enter into joint ventures with an out-of-state institution to conduct trust business.\textsuperscript{118} Also, banks are being permitted to acquire out-of-state "industrial banks."\textsuperscript{119} Acquisition of mortgage companies by banks continues to grow. These acquisitions increased sixty-nine percent over the year ending June 30, 1982.\textsuperscript{120} In 1982, Congress also passed legislation intending to expand the banking industry's role in international commerce. The new bill permits the banking industry to invest in export trading companies (organizations that export U.S. goods and services and provide related activities).\textsuperscript{121} Thrift institutions across the country are also offering a wide range of services. The continuing deregulation of depository institutions is opening up a whole range of powers to thrifts, while also forcing them to compete with a wide range of financial services organizations.

V. CONCLUSION

Removal by state legislators of barriers to interstate branching by banks, technological advancements, shifts in regulatory position concerning inter-industry and interstate acquisitions and Congress' relaxing of restraints on similar transactions all demonstrate the general mood toward deregulation of the banking industry in the 1980's, that general attitude being to take definite steps to remove the fence which has divided the banking industry, on a geographic basis, as well as separating the industry according to financial services available.

Some members of the legal profession believe that barriers to interstate banking are not going to be removed in the near future. However, bankers are expected to continue to circumvent the laws. If Congress does eventually authorize interstate banking, it will do so by permitting either contiguous state arrangements or reciprocal agreements between states. De facto repeal

\textsuperscript{117} Am. Banker, Dec. 8, 1982, at 2, col. 1.
\textsuperscript{118} Am. Banker, Nov. 12, 1982, at 14, col. 4.
\textsuperscript{120} Am. Banker, Oct. 12, 1982, at 1, col. 2.
by the marketplace of the McFadden Act and Douglas Amendment, which restrict the location of bank branches and the banking subsidiaries of bank holding companies to a single state, is likely to occur before Congress repeals those acts de jure. The McFadden Act will, in all likelihood, be removed or amended within the next several years.

The 1982 Depository Institutions Act Amendments was preceded by the Carter Administration’s Report on Geographic Restrictions on Commercial Banking in the United States, which also contained recommendations which would erode McFadden and Douglas limitations. The report recommended that electronic fund transfer (EFT) terminals not be subject to “brick and mortar” branching statutes. The report also recommended that a bank holding company be permitted to acquire a large failed bank in another state. Finally, a gradual relaxation of the prohibition against interstate bank holding company acquisitions was proposed. In a remark about geographic restraints on banking, the Report concluded that:

> the failure to liberalize the present framework will perpetuate the existing discrimination against the retail customer, deprive the public of the benefits of increased competition, impede the efficient allocation of new technologies, and restrict the ability of bank management to compete with other, nonbank financial institutions playing under a different set of rules.

It will not be easy to undo years of development largely influenced by regulations. There is a problem of “protected turf.” The McFadden and Douglas Amendment interstate restrictions combined with restrictive state laws on branching have been viewed by some as helping to foster and preserve small banks. Fears have been repeatedly voiced that the growth of interstate banking will lead to widespread failures and consolidation of small commercial banks and that because these banks are particularly sensitive to the needs of small business, the opportunities for these small businesses to obtain financing and services will be significantly curtailed.

Some areas may experience reductions in small business financing and financial services as a result of interstate banking. However, increases in services could be even more important. New opportunities for small business financing will arise as a result of increased competition, both geographically and across lines of business. The new trends and changes occurring in the banking industry may not result in as much damage to small banks as initially anticipated.

Small commercial banks are providing consumer services to geographically diverse regions through shared arrangements. Where banks outside

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122 Raven, supra note 77, at 400.
123 Id. at 401.
one territory enter another and do provide services to small business, the increased competition will be a plus for the new clients. Shrinkage which occurs in indigenous firms typically will be more than offset by benefits to small business from the improvements in competition and availability of services permitted by reduced barriers. New sources of small business financing and services can also be expected as a host of non-bank firms rediscover the small businessman. Larger banks are also rediscovering small business, and since they are not large enough to crowd out the small bank opportunities in the small business market, they will provide an additional source of financing.

An important issue surrounding geographic deregulation surfaces when banking organizations enter a new market. Generally speaking, a relaxation of restraints results in an increase in the number of banking facilities and a wider variety of banking services. Short-term price benefits for the public are likely to occur. On the other hand, some argue against relaxing these restrictions on the ground that it would lead to a concentration of banking resources. Of course, it is true that "measured" concentrations would increase at the state levels. But there are adequate public policy safeguards to prevent undue or excess concentration, and increased statewide concentration does not preclude meaningful competition in local markets. 125

A new position favored by some federal regulators and members of Congress concerning the future structure of the banking industry is to give banks expanded powers through a holding company framework rather than to allow banks to conduct the new activities directly. Bankers oppose such a proposal because they view the subsidiary format as too cumbersome, costly, and unnecessary for the safety and soundness of banks.

The holding company format for new powers might prove to be a better system because it permits management to set up the new activities in separate profit centers and allows the establishment of different compensation systems for different specialties. The format makes possible some variation in corporate culture and may even make it easier to attract good people to lead and to staff the subsidiary companies. The holding company structure permits the isolation of higher risk activities from traditional banking functions, allowing bank subsidiaries and their non-bank activities to be under the same regulatory framework. Because of the concern for the risks associated with banking activities as well as public policy concerns about the safety and soundness of the banking system, Congress will be less likely to withhold the expanded powers from BHCs than they would from the individual banks.

Prospects that banks will also enter the securities industry are faced with the strongest opposition. Congressional leaders in the field of bank-

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125 Raven, supra note 77, at 402.
related legislation are afraid that bank entry into the securities business could result in undue concentration of financial institutions and result in a threat to bank safety and soundness. All of these competitive forces, together with the shifts in regulatory policy and the general movement toward deregulation which are taking place in the banking industry today, are laying a foundation for a strong regional industry of tomorrow.