8

Office of Thrift Supervision
Department of the Treasury

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The Honorable Harvey L. Pitt
Chairman
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D.C. 20548

Dear Chairman Pitt:

Over the past several years we have discussed, with various representatives of the Securities and Exchange Commission, our view that savings associations should have parity with banks under the Securities Exchange Act of 1934 (1934 Act) and the Investment Advisers Act of 1940 (IAA). In its interim final broker-dealer rule, the Commission agreed that parity was appropriate in the key area of broker-dealer registration under the 1934 Act (see Rule 15a-9). As support for this exemption, the SEC explained in the preamble that the differences between banks and savings associations have narrowed, savings associations are subject to a similar regulatory structure and examination standards as banks, and it is reasonable to afford savings associations the same type of exemptions that banks have from broker-dealer registration.

While we applaud the significant steps taken in the interim final rule to narrow the gap between savings associations and banks under the 1934 Act, we have identified several other issues. We urge the SEC to quickly address, through administrative action, the remaining discrepancies in treatment between savings associations and banks. We also urge the SEC to support legislation the Office of Thrift Supervision (OTS) has provided to the House Financial Services Committee in response to its request for regulatory burden reduction proposals. This proposal would give savings associations parity with banks under the various securities laws. A copy of our draft legislation is enclosed, accompanied by a detailed justification.

Securities Exchange Act of 1934

One remaining discrepancy under the 1934 Act concerns collective investment funds. The Gramm-Leach-Bliley (GLB) Act exempted savings association common trust funds from 1934 Act registration requirements, but it did not include the necessary amendment to give savings association collective investment funds the same exemption that applies to banks. We have no reason to think that Congress intended different treatment for bank and savings association collective investment funds, nor is there any logic to treating them differently.

One way to correct this anomaly is for the SEC to exercise its exemptive authority to treat savings associations and banks the same for all purposes under the 1934 Act. OTS also supports a statutory amendment to the definition of bank in the 1934 Act to conform to the definition of bank in the Investment Company Act of 1940, as amended by section 223 of the GLB Act.

Section 3(a)(34), which defines appropriate regulatory agencies for various oversight purposes, should also be amended to make OTS the designated appropriate regulatory agency for the institutions it supervises for purposes of subparagraphs (A) through (D) as well as (F).

Investment Advisers Act of 1940

Another area where savings associations are treated differently than banks is under the IAA. In the summer of 2000, during the mark-up hearing for S. 2107, the "Competitive Market Supervision Act," Senator Bayh considered offering an amendment to the IAA to extend the bank registration exemption to savings associations. Based on representations that the SEC planned to resolve this anomaly administratively, he did not offer the amendment. While the SEC has announced its intention to address this unequal treatment and has initiated a regulation project, it has not published any proposed changes. Savings associations are placed at a competitive disadvantage to banks because they must register with the SEC when performing the same activities banks perform without having to register. For this reason, some savings associations have recently converted to bank or state trust company charters to obtain the benefit of the registration exemption. As the SEC has stated in the context of the broker dealer regulations, extending the exemption for banks to savings associations is necessary or appropriate, in the public interest, and is consistent with the protection of investors. We hope the SEC will take action in the near future to extend this logic by giving savings associations parity with banks under the IAA.

We will be calling you soon to arrange a meeting to discuss expediting solutions to these problems. OTS supports administrative action that would establish parity by use of the SEC's exemptive authority to treat savings associations the same as banks under all the securities laws. We also believe that conforming statutory amendments are appropriate. I hope we can enlist your support to make these much needed changes.

Sincerely yours,

Ellen Seidman
Director

Enclosure

(Submitted to House Financial Services Committee on 10/2/2001)

PARITY FOR THRIFTS UNDER THE INVESTMENT ADVISERS ACT OF 1940 AND THE SECURITIES EXCHANGE ACT OF 1934.

Section ____ amends the Investment Advisers Act of 1940 (IAA) and the Securities Exchange Act of 1934 (1934 Act) to give thrifts parity with banks with respect to investment adviser and broker-dealer registration requirements and for various other purposes. It also makes a minor conforming amendment to the Investment Company Act of 1940 (ICA).

The bill broadens the definition of the term "bank" in the IAA and the 1934 Act to cover federal and state savings associations. The definition of "applicable regulatory agency" in the 1934 Act is also amended to add OTS for the institutions it regulates, analogous to the authority of the OCC, the Federal Reserve Board, and the FDIC for their institutions.

Thrifts focus activities primarily on residential, community, small business, and consumer lending under the Home Owners' Loan Act (HOLA). When they do engage in investment adviser, broker-dealer, and other activities under the IAA and the 1934 Act, however, there is no logical basis to treat the regulatory oversight of thrifts and banks differently. The SEC has already removed the disparity in treatment for broker-dealer registration in its interim final rule published on May 18, 2001 (discussed in more detail in connection with the detailed discussion of the 1934 Act amendments, below). SEC staff have made various public statements that the SEC is also seriously considering removing the disparity for purposes of the IAA.

This section enacts parity, affirming the SEC's recent and upcoming administrative actions with a statement of Congress's intent, and makes other conforming changes. These amendments will also eliminate the incidental differences that remain, as explained below, and avoid the need for a series of SEC administrative exemptions as additional differences come to light.

Detailed Justification

Treating thrifts and banks the same under the securities laws makes sense for the following reasons:

- Thrifts and banks provide investment adviser, trust and custody, and third party brokerage services in the same manner, but are subject to different requirements under the SEC's interpretation of the securities laws. To the extent thrifts are subject to different rules and must register with the SEC, they are placed at a competitive disadvantage to banks due to the additional costs. For this reason, some thrifts have recently converted to a bank or state trust company charter to obtain the benefit of the registration exemption under the IAA. This allows them to side step SEC regulation with a one-time

conversion cost. It is sound public policy to treat the bank and thrift charters the same where similarly situated. This approach also promotes a level playing field in the marketplace.

- OTS examinations of these activities are already conducted in the same manner as those of the other banking agencies. OTS is in the process of formalizing these policies with new regulations and guidance. For example, in August, OTS issued an entirely revised trust and asset management handbook. This reinforces that under OTS's regulations and examinations thrift customers have protections equivalent to those the other banking agencies provide for bank customers.

- The statutory authorities for thrifts and banks to engage in trust services are essentially the same. In 1980, Congress gave thrifts the authority to offer trust services closely based on the authority it gave to national banks in 1962.[1] The Senate report for the Depository Institutions Deregulation and Monetary Control Act of 1980 explained that the HOLA amendment gives thrifts "the ability to offer trust services on the same basis as national banks."[2] Consistent with this legislative history, these amendments promote uniformity in the way thrifts and banks provide trust services.

- The GLB Act amended the definitions of broker and dealer in the 1934 Act by removing the banks' blanket exemption from broker-dealer registration requirements and replacing it with a list of activities a bank may engage in directly without registering. Other activities must be "pushed out" to a broker-dealer. As noted above, the SEC has already recognized that these exempt activities are just as appropriate for thrifts. These include trust and custodial activities, entering into third party brokerage arrangements[3], offering sweep accounts where the balance is swept directly (instead of through a broker-dealer) into a no-load money market mutual fund, and effecting transactions in municipal securities.

- Securities firms that provide investment advisory or broker-dealer services by contract with thrifts and banks will not have the regulatory burden of having to follow different rules, depending on whether a thrift or a bank is involved. Where different rules apply, additional compliance costs are borne by thrifts and banks and, ultimately, by their customers.

- Wherever possible, the banking agencies have set uniform standards to protect consumers where their regulated financial institutions are engaged in exactly

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[1] See section 5(n) of HOLA (12 U.S.C. § 1464(n)) for thrifts and 12 U.S.C. § 92a for banks.

[2] S. Rep. No. 96-368, at 13 (1979), reprinted in 1980 U.S.C.C.A.N. 236, 248.

[3] Since 1993, the SEC has permitted a thrift to enter into third party brokerage arrangements without having to register as a broker under the 1934 Act if it complies with the conditions in a no-action letter referred to as the "Chubb letter." The conditions the GLB Act imposes on banks that enter into third party brokerage arrangements are quite similar—but not identical—to those in the Chubb letter.

the same activities, in the same manner. If thrifts and banks are subject to different rules by the SEC, the banking agencies will not be able to establish a uniform regulatory scheme and a level playing field.

Section-By-Section Summary and Explanation

Securities Exchange Act of 1934

The 1934 Act governs the trading, purchase, and sale of certain securities, including the registration of broker-dealers and securities subject to the Act. The landscape governing the regulation of broker-dealers in the bank and thrift context is undergoing significant change. Before the GLB Act, banks had a blanket exemption from broker-dealer registration requirements under the 1934 Act, but thrifts did not. Under the GLB Act, banks lost their blanket exemption and instead may engage only in specified activities without registering. Other activities must be "pushed out" to a registered broker-dealer. The relevant provisions of the GLB Act were to have taken effect on May 12, 2001.

The SEC issued interim rules on May 11, 2001 (published in the Federal Register on May 18), implementing the new "push-out" requirements, generally giving banks until October 1, 2001, to comply with the new rules. As part of this rule, the SEC used its exemptive authority to apply the same rules to thrifts as apply to banks for purposes of broker-dealer registration, giving thrifts parity with banks for the first time. In response to extensive negative responses to "push-out" requirements in the SEC rule from the bank regulators and the banking industry, the SEC delayed the effective date of the rule until May 12, 2002, and gave banks and thrifts a blanket exemption from the definitions until May 12, 2002. Until then, banks and thrifts may engage in broker-dealer activities without registering with the SEC.

Subsection (a)(1) amends the definition of bank in the 1934 Act to cover depository institutions as defined in the Federal Deposit Insurance Act. This broadens the definition to include federal and state savings associations. This change codifies the actions the SEC took in its May 11 interim final rule to extend the new definitions of broker and dealer to apply to thrifts in addition to banks. The new definition is the same as the definition of bank in the Investment Company Act of 1940 (ICA), as amended by section 223 of the Gramm-Leach-Bliley (GLB) Act. The amended term also includes a branch or agency of a foreign bank, as defined in the International Banking Act of 1978, consistent with the ICA, as amended by the GLB Act.

By treating thrifts and banks the same under the 1934 Act, the amendment will assure equal treatment of banks and thrifts without having to rely on case-by-case action by the SEC. While the May 11 rule goes a long way towards achieving parity, it leaves several gaps. For example, the GLB Act amended the definition of "exempted security" in section 3(a)(12)(A)(iii) of the 1934 Act. Before the GLB Act, only bank common trust

funds[4], not thrift common trust funds, were exempt from the security registration requirements of section 12 of the 1934 Act. Under the amendment, any common trust fund excluded from the definition of investment company under the ICA is exempt. Because the GLB Act amended the definition of bank in the ICA to cover depository institutions generally, it indirectly extended the bank common fund exemption to include thrift common trust funds. The GLB Act did not, however, amend the very next provision, clause (iv), which exempts collective trust funds[5] maintained by a bank. There is no apparent reason to treat banks and thrifts the same for purposes of common trust funds but differently for purposes of collective trust funds. Amending the definition of bank will eliminate this unintended result and other potential problems that are likely to arise.

Besides amending the definition of bank, several additional changes are needed to achieve full parity. Subsection (a)(2) makes several changes to the definition of appropriate regulatory agency in section 3(a)(34) of the 1934 Act. Under subparagraph (G) of the definition, OTS is already the appropriate regulatory agency with respect to a government securities broker or dealer or an associated person which is also a savings institution, and the other banking agencies are the appropriate regulatory agencies for the institutions they supervise. OTS should be added to the following other categories as the designated appropriate regulatory agency for the institutions it supervises:

- A municipal securities dealer (subparagraph (A)).
- A clearing agency or transfer agent (subparagraph (B)).
- A participant or applicant to become a participant in a clearing agency or a person requesting or having access to services offered by a clearing agency (subparagraph (C)).
- An institutional investment manager that is a bank the deposits of which are insured in accordance with the Federal Deposit Insurance Act (subparagraph (D)). (Subsection (a)(1) broadens the definition of bank to include thrifts.)
- A person exercising investment discretion with respect to an account (subparagraph (F)).

Section 34(a)(34)(H) is not being amended to add OTS because it relates to special purpose banks, not thrifts.

Investment Advisers Act of 1940

The IAA generally exempts banks from the registration and other requirements of the IAA by excluding them from the definition of investment adviser. To extend this exemption to thrifts, for the reasons already described, subsection (b)(1) makes the same

[4] Trust assets may be invested in a common trust fund established by a depository institution. Using a common trust fund reduces administrative costs and promotes diversification, especially for smaller trusts.

[5] Section 401(k) accounts may be invested in collective trust funds established by a depository institution. Using a collective trust fund reduces administrative costs and promotes diversification, especially for smaller accounts.

change to the definition of bank in the IAA as subsection (a) makes to the definition of bank in the 1934 Act.

The exemption does not apply to institutions that advise registered investment companies, such as mutual funds. Where a separately identifiable department or division of a bank advises an investment company, the IAA requires registration of the department or division, not the whole institution. The same rules will apply to thrifts.

Subsection (b)(2) makes conforming amendments to the interagency consultation provisions of the IAA, added by section 220 of the GLB Act, by adding references to savings and loan holding companies to parallel the existing references to bank holding companies.

Investment Company Act of 1940

The Investment Company Act of 1940 (ICA) requires SEC registration of investment companies, such as mutual funds. Banks and thrifts have long been exempt from the definition of investment company under section 3(c)(3) of the ICA. Bank common trust funds have also been exempt, but, until the GLB Act, thrift common trust funds were not. The GLB Act amended the definition of bank to include depository institutions, including thrifts. The effect of this change was to give thrift common trust funds and similar funds the same ICA exemption that has applied to bank funds, including the new limitations on the exemption added to the definition of investment company by section 221(c) of the GLB Act.

One additional conforming change, however, is still needed. Subsection (c) amends section 10(c) of the ICA, concerning the limitation on the membership of investment company boards by officers, directors, or employees of any one savings and loan holding company, to parallel the existing treatment of bank holding company officers, directors, and employees. This corrects an oversight that occurred when section 213(c) of the GLB Act amended section 10(c) of the ICA.

AMENDMENT

SEC. ____. PARITY FOR THRIFTS UNDER THE INVESTMENT ADVISERS ACT OF 1940 AND THE SECURITIES EXCHANGE ACT OF 1934.

(a) SECURITIES EXCHANGE ACT OF 1934.

(1) DEFINITION OF BANK.—Section 3(a)(6) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(6)) is amended by striking "(A) a banking institution organized under the laws of the United States" and inserting "(A) a depository institution (as

defined in section 3 of the Federal Deposit Insurance Act) or a branch or agency of a foreign bank (as such terms are defined in section 1(b) of the International Banking Act of 1978)".

(2) **INCLUDE OTS UNDER THE DEFINITION OF APPROPRIATE REGULATORY AGENCY FOR CERTAIN PURPOSES.**—Section 3(a)(34) of such Act (15 U.S.C. 78c(a)(34)) is amended—

(A) in subparagraph (A)—

(i) in clause (ii), by striking "(i) or (iii)" and inserting "(i), (iii), or (iv)";

(ii) by striking "and" at the end of clause (iii);

(iii) by redesignating clause (iv) as clause (v); and

(iv) by inserting the following new clause after clause (iii):

"(iv) the Director of the Office of Thrift Supervision, in the case of a savings association (as defined in section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)) the deposits of which are insured by the Federal Deposit Insurance Corporation, a subsidiary or a department or division of any such savings association, or a savings and loan holding company; and";

(B) in subparagraph (B)—

(i) in clause (ii), by striking "(i) or (iii)" and inserting "(i), (iii), or (iv)";

(ii) by striking "and" at the end of clause (iii);

(iii) by redesignating clause (iv) as clause (v); and

(iv) by inserting the following new clause after clause (iii):

"(iv) the Director of the Office of Thrift Supervision, in the case of a savings association (as defined in section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)) the deposits of which are insured by the Federal Deposit Insurance Corporation, or a subsidiary of any such savings association, or a savings and loan holding company; and";

(C) in subparagraph (C)—

(i) in clause (ii), by striking "(i) or (iii)" and inserting "(i), (iii), or (iv)";

(ii) by striking "and" at the end of clause (iii);

(iii) by redesignating clause (iv) as clause (v); and

(iv) by inserting the following new clause after clause (iii):

"(iv) the Director of the Office of Thrift Supervision, in the case of a savings association (as defined in section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)) the deposits of which are insured by the Federal Deposit Insurance Corporation, a savings and loan holding company, or a subsidiary of a savings and loan holding company when the appropriate regulatory agency for such clearing agency is not the Commission; and";

(D) in subparagraph (D),

(i) by striking "and" at the end of clause (ii);

(ii) by redesignating clause (iii) as clause (iv); and

(iii) by inserting the following new clause after clause (ii):

"(iii) the Director of the Office of Thrift Supervision, in the case of a savings association (as defined in section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)) the deposits of which are insured by the Federal Deposit Insurance Corporation; and";

(E) in subparagraph (F),

(i) by redesignating clauses (ii), (iii), and (iv) as clauses (iii), (iv) and (v), respectively; and

(ii) by inserting the following new clause after clause (i):

"(ii) the Director of the Office of Thrift Supervision, in the case of a savings association (as defined in section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)) the deposits of which are insured by the Federal Deposit Insurance Corporation; and"; and

(F) at the end of the last undesignated paragraph, by inserting the following new sentence: "As used in this paragraph, the term 'savings and loan holding company' has the meaning given it in section 10(a) of the Home Owners' Loan Act (12 U.S.C. 1467a(a))."

(b) INVESTMENT ADVISERS ACT OF 1940.

(1) DEFINITION OF BANK.—Section 2(a)(2) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(2)) is amended by striking "(A) a banking institution organized under the laws of the United States" and inserting "(A) a depository institution

(as defined in section 3 of the Federal Deposit Insurance Act) or a branch or agency of a foreign bank (as such terms are defined in section 1(b) of the International Banking Act of 1978)".

(2) **CONFORMING AMENDMENTS.**—Subsections (a)(1)(A)(i), (a)(1)(B), (a)(2), and (b) of section 210A of such Act (15 U.S.C. 80b-10a), as added by section 220 of the Gramm-Leach-Bliley Act, are each amended by striking "bank holding company" each place it occurs and inserting "bank holding company or savings and loan holding company".

(c) **CONFORMING AMENDMENT TO THE INVESTMENT COMPANY ACT OF 1940.**—Section 10(c) of the Investment Company Act of 1940 (15 U.S.C. 80a-10(c)), as amended by section 213(c) of the Gramm-Leach-Bliley Act, is amended by inserting after "1956)" the following: "or any one savings and loan holding company (together with its affiliates and subsidiaries) (as such terms are defined in section 10 of the Home Owners' Loan Act)".