November 12, 1993

MEMORANDUM FOR BOB RUBIN

THROUGH: SYLVIA MATHEWS

FROM: ELLEN SEIDMAN

SUBJECT: BANK REGULATOR CONSOLIDATION

On Wednesday, Frank Newman, Gene Ludwig, Treasury, OCC and OMB staff and I met to discuss bank regulator consolidation. Frank is scheduled to testify on the subject before Senator Riegle -- in long-scheduled testimony -- on Wednesday morning. Senators Riegle and D'Amato have submitted a bill to fully consolidate the four banking regulators into a new independent[1] Federal Banking Commission, and have essentially challenged -- in a joint letter with Chairman Gonzalez -- the Administration to move quickly and effectively in this area.

Frank and Gene had been talking to Chairman Greenspan and Governor LaWare about this issue over the past several months. For reasons mainly relating to prestige, turf, and the desire to keep the Reserve Banks in business, Greenspan and LaWare have said their position is that the Fed should retain independent regulatory and supervisory authority over a relatively large number of large institutions (they have a formula that apparently yields about 70 to 100 institutions) and over all bank holding companies where the lead bank is a state member bank. Other bank holding companies -- mainly those with lead national banks -- would be regulated and supervised by a new, independent banking regulator. Thus, a dual federal regulatory system would be retained. Both Gene and Frank are also concerned that this system would lead to increased (there already is some) regulatory forum-shopping, with the new bank regulator as the loser.

At the meeting, the group unanimously agreed that the Fed proposal, while representing interesting movement, was, and would be seen on the Hill as, a Rube Goldberg machine that did not really solve any of the serious problems of multiple regulators. We concluded that the Administration should support something much closer to Riegle/D'Amato/Gonzalez, namely:

- Full consolidation of the OCC and OTS into a new Federal Banking Commission (FBC)

[1] The Commission would be governed by a five-member board. The Board would consist of a Chairman appointed by the President with Senate advice and consent for a five-year term, the Secretary of the Treasury or his designee, a Governor of the Fed, and two other presidentially-appointed independent members.

- Movement of all bank supervisory functions of the FDIC into the new FBC. The FDIC would remain the insurer, and would have limited backup examination authority, mainly for banks showing some signs of distress. It would have no regulatory authority other than that directly related to the insurance function.

- Movement of all bank supervisory functions of the Fed, including bank holding company supervision, into the new FBC, but with authority for the Fed to conduct joint examinations of up to 25 entities, with the Fed to choose the entities based on their importance to the payment system. The discount window function, all monetary policy and oversight and operation of the payment system would remain with the Fed.

- State-chartered non-member banks would continue to be examined by states, probably under some sort of FBC certification system.

- The FBC would be governed by a five-member board, consisting of a Chairman appointed by the President for a four-year term roughly coterminous with his (e.g., ending March 31 of the year after an election), subject to Senate confirmation, two representatives of the Treasury (who would be ex officio advice and consent appointees); a member of the Fed Board of Governors; and one independent appointed by the President. We discussed, but did not fully settle on, the idea that the Fed member might be designated Vice Chairman, but without power to succeed to the Chairmanship. I am also not fully comfortable with the notion of two Treasury representatives for a number of reasons (one simply being the amount of time they will be able to devote to it, another being the political optics of the proposal), but as a going-in position it might be OK.

- For a specified period of, say, three years, the FBC would be required to operate separate divisions for national banks, community banks, and possibly thrifts. After the period, it could reorganize itself.

- The FBC could have up to four advisory committees.

- Picking up the Riegle effective dates, the Secretary of the Treasury would essentially determine when the switch would be effective, between 6 and 10 months after the bill was enacted, but he could extend that for another 5 months.

- There would be some employee buyouts and some employee protections, but after some reasonable period of time, the FBC could reduce its workforce.

- Ultimately, all banks would pay fees to the FBC for examination. However, during some transition period, the Fed would pay the FBC for banks and holding companies it previously supervised and the FDIC would pay for banks it supervised. The new system should ultimately have a positive revenue impact because it would eliminate the Treasury subsidy of examination of state non-member banks.