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CREATOR: Alice Veenstra (CN=Alice Veenstra/OU=OMB/O=EOP [OMB])

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SUBJECT: Treasury Testimony on Financial Services Modernization

TO: Michael Deich (CN=Michael Deich/OU=OMB/O=EOP @ EOP [OMB])

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CC: Daniel M. Tangherlini (CN=Daniel M. Tangherlini/OU=OMB/O=EOP @ EOP [OMB])

READ:UNKNOWN

CC: Michelle A. Enger (CN=Michelle A. Enger/OU=OMB/O=EOP @ EOP [OMB])

READ:UNKNOWN

CC: Alan B. Rhinesmith (CN=Alan B. Rhinesmith/OU=OMB/O=EOP @ EOP [OMB])

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TEXT:

Michael,

Michelle Enger and Alice Veenstra attended the House Banking Committee hearing yesterday on financial services modernization at which Secretary Rubin and Undersecretary Hawke testified. Representatives LaFalce, Roukema and Vento commented on the tardiness of the proposal and Rep. Vento expressed significant disapproval of the two-option model.

Chairwoman Roukema stated that the operating subsidiary and WFI proposals have caused division among trade groups regarding financial services modernization. I believe she was referring to recent action by the OCC to consider broader powers for national banks in their operating subsidiaries. Rep. Vento stated that it is imperative that we merge the deposit insurance funds.

Questions Asked

Chairman Leach asked Treasury if they agreed with the unanimous opinion of the five regulators (OCC, OTS, Fed, FDIC, and SEC) for the need to merge OTS and OCC, BIF and SAIF and the bank and thrift charters. Secretary Rubin said it depended on which option Congress adopted. Chr. Leach also asked if WFI access to the payment window was subsidizing corporations and making the payment system more complicated. Secretary Rubin responded that WFI's are regulated, highly capitalized banks and that corporations will not have access to the payment system.

Chr. Roukema asked if Treasury really supports a basket approach, what was the status of umbrella regulation, and what was the Administration's response to charges that it was going "beyond Barnett" and destroying functional regulation and opposing the SEC. Treasury responded that we support both options equally and see the "banking and commerce" issue as a cultural one, not an economic one that is better decided by Congress, that we support an umbrella regulator, that we support state regulation of insurance and that we have worked closely with the SEC to develop this proposal. Undersecretary Hawke spent some time explaining how the state insurance regulation preemption would work. A number of Members asked for clarification on what type of state insurance laws would be pre-emptable as discriminatory.

Rep. Vento asked a series of questions about how grandfathering of the thrifts and divestiture of non-financial assets would work.

The Democrats (particularly Congressional Black Caucus Members) seemed very concerned about how consumers (especially those in underserved areas) would get benefit from the Administration's financial services modernization proposal. Rep. Waters wanted to know why the Administration did not use this opportunity to expand consumer protections. Many were concerned that Treasury's proposal would allow institutions to move assets around more easily in order to avoid CRA coverage. Treasury pointed out that that is exactly why they propose to apply CRA to wholesale financial institutions (WFIs). Secretary Rubin stressed that financial services modernization would provide more competition which is better for consumers. When Rep. Cook pressed Treasury on the Administration's willingness to modify CRA for WFI's, the Secretary stood firm that CRA was not up for grabs.

CDFI Questions

Rep. Riley used the hearing as an opportunity to question Secretary Rubin about the current investigations of the CDFI Fund by the Banking's General Oversight and Investigations Subcommittee. He asked why Treasury had not yet adequately responded to the Subcommittee's requests for information, and asked when the Subcommittee should expect to receive a response. Secretary Rubin said the Subcommittee questions had been referred to the Treasury IG. Rep. Riley stated that he could see no reason to provide the CDFI Fund with any additional appropriations until Treasury could provide satisfactory answers to the

Subcommittee's investigation.

Items that the Administration was asked to follow-up on

Rep. Watt asked for copy of the CRA language that applies to wholesale institutions.

Rep. Waters on behalf of the Congressional Black Caucus members asked Treasury to directly address a number of questions posed by Consumers Union in a report regarding consumer protections in our proposal.

Rep. Vento asked Treasury to distinguish between allowable commercial equity holdings associated with merchant banking and disallowed non-financial holdings.

Mark-Up

Chairman Leach stated he will produce a bill for mark-up on Friday and that the mark-up will be held next Wednesday or Thursday (June 11 or 12).

- Alice Veenstra and Michelle Enger