Federal Reserve Bank of Philadelphia

BANKING LEGISLATION & Policy

January-March 1999

Volume 18, Number 1

CONTENTS

Recent Developments

Regulators Come to Terms Over Treatment of Loan Loss Reserves

On March 10, the federal banking agencies and the Securities and Exchange Commission (SEC) issued a joint letter ending the confusion over conflicting regulatory views on loan loss reserves. The regulators announced plans to establish a joint working group whose mission would be to provide the agencies with information on the practices used by banks when determining their allowance for credit losses. This information would be used by the agencies to issue uniform guidelines on loan loss reserves for their financial institutions. As part of the settlement, the SEC has promised not to require depository institutions to restate earnings even if it believes that allowances were overstated. This compromise has headed off legislative initiatives to end the bank loan loss controversy that began last year with acquisition of Crestar Financial Corporation by Sun Trust Banks Inc. [See *Banking Legislation and Policy,* Fourth Quarter 1998, for more information on the origins of this dispute.]

Passage of Financial Services Reform Uncertain

On March 11, the House Committee on Banking and Financial Services approved a compromise version of the financial services reform bill, H.R. 10. Although the compromise bill was voted from committee with strong support (51-8), the prospects for enactment this year are doubtful. The reported bill attempts to find a middle ground in the dispute between the Board of Governors and the Treasury Department over the appropriate structure for financial firms with expanded powers. In the House bill, insurance sales and investment and merchant banking activities would be carried out through bank subsidiaries. Real estate development and insurance underwriting would be carried out through holding company subsidiaries.

Although Treasury Secretary Rubin has endorsed the compromise, the Board of Governors has maintained its position that investment banking and merchant banking activities should be housed in subsidiaries of the bank's holding company, rather than bank operating subsidiaries. Furthermore, Senate Banking Committee Chairman Phil Gramm, who has pushed his own version of a modernization bill through committee, has made known his displeasure with H.R. 10's Community Reinvestment Act (CRA) provisions. The CRA modifications incorporated by Senator Gramm into the Financial Services Modernization Act of 1999, especially the repeal of CRA for small rural banks, have elicited a strong response from Democratic legislators and the Executive Branch. That bill won passage along a strict party-line vote in the Senate Committee on Banking, Housing and Urban Affairs. President Clinton, in early March, threatened a veto of Senator Gramm's bill as a result of the CRA rollbacks and other disputed provisions.

The major provisions of both the House and Senate financial modernization bills are summarized below.

SUMMARY OF FEDERAL LEGISLATION

New Legislation

1. Financial Services Act of 1999 (H.R. 10). Introduced by Representative Leach (R-IA) on January 6, 1999. Related Bills: H.R 665, H.R. 823, S. 753.

Status: Reported out of the Committee on Banking and Financial Services on March 23, 1999. Also referred to the Committee on Commerce.

This bill would allow banks to affiliate with insurance and securities firms in financial holding companies (FHCs). For the most part, only activities determined to be financial in nature could be undertaken by FHCs. These activities would include, but not be limited to: 1) commercial banking; 2) insurance operations, including the underwriting of insurance; 3) securities operations; 4) investment advisory services; 5) money transmitting services; and 6) real estate development. The Board of Governors of the Federal Reserve System (Federal Reserve Board) and the Department of the Treasury would be jointly responsible for making determinations as to whether a new activity is financial in nature. The bill would also permit FHCs to carry out activities incidental to or complementary to financial activities. The inclusion of complementary activities has not appeared in previous versions of H.R. 10.

Real estate development and insurance underwriting could be carried out only through holding company subsidiaries, while insurance sales and investment and merchant banking could be carried out through operating subsidiaries of banks. The Federal Reserve Board would have the final say on whether new merchant banking activities could be carried out directly though bank subsidiaries or only through a holding company subsidiary.

The Federal Reserve Board would be the chief regulator of FHCs. National banks with assets over $10 billion and with subsidiaries engaged in nonbank activities would be required to organize as a holding company. Supervising and monitoring of financial institutions must be done in a manner that reduces the regulatory burden on the institutions. Thus, the Federal Reserve Board would be required to use public information or reports already on file with an institution's functional regulator before requesting the information from the institution. In general, the Federal Reserve Board would not be permitted to impose capital requirements on nonbank affiliates.

The bill would also allow for the creation of Wholesale Financial Institutions (WFIs) and Wholesale Financial Holding Companies (WFHCs). In general, a WFI would be a bank that takes deposits in excess of $100,000. It would be an uninsured depository institution but would have access to the Federal Reserve discount window and be supervised by the Federal Reserve Board. The bill would allow only 10 WFIs to retain access to the discount window and payment system. A WFHC would be a domestic holding company controlling at least one WFI and no other insured depository institution. A WFHC would also have to be primarily engaged in financial activities and would be able to maintain its commercial activities for up to 10 years, provided that the revenues from these commercial activities account for less than 15 percent of WFHC revenues.

The creation of new unitary thrifts would be prohibited, but thrifts currently in operation and those with applications pending as of February 1999 would be grandfathered. The bill would allow these thrifts to be sold to commercial firms. According to the OTS, as of December 1998, there were 525 firms that met these criteria.

Finally, the modernization bill incorporates provisions to protect the privacy of bank customers and makes changes to the Federal Home Loan Bank System. Attempts to gain customer financial information from a financial institution by presenting false credentials would be illegal. The Federal Home Loan Bank Act would be amended to make community financial institutions (CFIs) eligible members, thus expanding commercial banks' access to the Home Loan Bank system. A CFI would qualify to be a Home Loan Bank member if it has insured deposits and less than $500 million in assets. It would not be required to meet the qualified thrift test of having at least 10 percent of its portfolio dedicated to home mortgages. CFIs would be able to secure advances from their Home Loan Bank to make small-business, agricultural, rural development, or low-income housing loans.

2. Financial Services Modernization Act of 1999. Introduced by Senator Gramm (R-TX).

Status: Approved by the Senate Committee on Banking, Housing and Urban Affairs on March 4, 1999.

The Senate version of financial modernization would allow bank holding companies (BHCs) to offer nonbank financial activities only through holding company subsidiaries, although BHCs or national banks with assets less than $1 billion would be permitted to offer these activities through bank subsidiaries. However, these exempt BHCs would be generally prohibited from underwriting insurance and real estate development activities. An activity would be considered financial only if both the Board of Governors of the Federal Reserve System (Federal Reserve Board) and the Treasury Department concurred.

Regulators would be required to request information and conduct examinations with an emphasis on lessening the regulatory burden on their respective institutions. The banking agencies would have to defer to the Securities and Exchange Commission (SEC) and state insurance authorities on matters relating to securities and insurance regulatory actions, respectively. No agency would be permitted to impose capital guidelines on an institution for which the agency does not have primary regulatory responsibility.

An institution would be CRA compliant if the institution's ratings over the past three years were "Satisfactory" or better. For example, a BHC could not be required to submit to a new CRA exam as a condition for approval of a merger. If a bank is deemed CRA compliant, an individual filing a CRA challenge to an institution's regulatory application to merge or undertake new activities would have to provide evidence that the institution was not meeting CRA requirements. In addition, CRA provisions would no longer apply to banks that are not located in metropolitan areas and that have less than $100 million in assets.

The bill would halt the creation of new unitary thrift holding companies, but unitary thrift applications on file as of February 1999 would be grandfathered.

Also, the bill would make community financial institutions (CFIs) eligible for advances from the Federal Home Loan Banks. CFIs are Home Loan Bank members with assets less than $500 million. They would be allowed to receive Home Loan Bank advances to make loans to small businesses, small farms, and small agribusiness.

3. Homeowners Insurance Availability Act of 1999 (H.R. 21). Introduced by Representative Lazio (R-NY) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would authorize the Secretary of the Treasury to set up a homeowners reinsurance program to lessen both state insurance programs' and private insurers' risks of insolvencies due to natural disasters. The Treasury would sign yearly reinsurance agreements with eligible state-operated insurance programs and private insurers. To be eligible to purchase these contracts, state-operated programs must fill a gap in the availability of private insurance within the state, must charge premiums sufficient to cover the actuarial costs of coverage, and provide coverage for a single natural disaster.

With some exceptions, the reinsurance contracts would require the state program or the regional insurance industry to sustain losses greater than $2 billion, and contracts would not be able to assign the Treasury more than 50 percent of the risk. The bill also sets a $25 billion yearly limit on claims paid out by the Treasury.

The Treasury Department would also be directed to set up a Disaster Reinsurance Fund to pay out claims to purchasers of reinsurance and to pay administrative costs of the program.

4. Financial Information Privacy Act of 1999 (H.R. 30). Introduced by Representative Leach (R-IA) on January 6, 1999. Related Bills: S. 187, H.R. 1339

Status: Referred to the Committee on Banking and Financial Services.

This bill would make it a federal crime for any person to provide false information to a financial institution to gain financial information about a customer of the institution. It would also be illegal to knowingly receive such financial information.

5. Teller Fee Relief Act (H.R. 114). Introduced by Representative DeLauro (D-CT) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Federal Deposit Insurance Act and the Federal Credit Union Act to make it illegal for a depository institution to charge a fee to a customer for using a service of the institution in person. For example, it would be illegal to charge a customer a fee to carry out a transaction with a bank teller.

6. Community Reinvestment Improvement Act of 1999 (H.R. 173). Introduced by Representative McCollum (R-FL) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Community Reinvestment Act (CRA) to reduce, and in some cases abolish, reporting requirements for small banks. An institution seeking a modified evaluation status could not: 1) have been in violation of the Equal Credit Opportunity Act during the five years preceding evaluation; 2) have received a 'needs to improve' or 'substantial noncompliance' rating in its most recent evaluation; and 3) have had assets of more than $500 million at the end of the previous year.

Qualifying institutions would not be required to provide regulators any information other than existing business records. Regulators would use this information along with testimony provided by interested groups to issue CRA grades. Also, any institution that had a CRA rating of "Outstanding" or "Satisfactory" within the past two years could not have a branch application denied on the basis of CRA compliance, unless the institution's compliance has seriously deteriorated.

Furthermore, institutions whose main office is located in an area with a population of less than 25,000 and whose total assets are less than $100 million would be exempt from complying with CRA.

7. Bank Examination Report Protection Act (H.R. 174). Introduced by Representative McCollum (R-FL) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Federal Deposit Insurance Act and the Federal Credit Union Act to safeguard confidential information gathered by the federal banking agencies. Supervisory information gathered by an agency would be considered privileged and could not be released without prior authorization from the agency. The bill would also grant state banking agencies and foreign bank regulatory authorities the same privacy privileges. Information requested by Congress or the Comptroller would be exempt from this restriction.

An individual seeking such information would need to make a request to the particular agency. If the request is denied, any further attempts to compel disclosure must be made in a federal court. A banking agency that appeals a federal court decision would be granted an immediate stay on a disclosure order pending the outcome of the appeal.

8. Credit Opportunity Amendments Act of 1999 (H.R. 190). Introduced by Representative McCollum (R-FL) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services and the Committee on the Judiciary.

This bill would amend the Community Reinvestment Act of 1977 by removing Community Reinvestment Act (CRA) examination ratings as a factor to be used by banking agencies when reviewing branch or merger applications from subject financial institutions.

The bill would also amend the Consumer Credit Protection Act (CCPA) and the Fair Housing Act (FHA) to include redlining as an illegal practice under the respective acts. Redlining is the practice in which a financial institution discriminates on the basis of the racial or ethnic characteristics of an applicant's neighborhood.

Statistical evidence of disparate treatment by itself would be insufficient to prove a redlining case. There must also be evidence showing the creditor intended to discriminate against a protected group in violation of the CCPA or the FHA.

9. Bulk Cash Smuggling Act of 1999 (H.R. 240). Introduced by Representative Roukema (R-NJ) on January 6, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This act would amend Title 31 of the United States Code to allow for the punishment of anyone who knowingly smuggles more than $10,000 into or out of the United States. A person convicted under this act would face a prison term of up to five years and would forfeit the money.

A person who could prove that the currency involved in the offense is derived from legitimate sources and intended for a lawful purpose would have the forfeiture penalty reduced to an amount proportional to the gravity of the offense.

10. Wire Transfer Fairness and Disclosure Act of 1999 (H.R. 382). Introduced by Representative Gutierrez (D-IL) on January 19, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Electronic Fund Transfer Act (EFTA) to require that all businesses that perform international money transfers disclose both the exchange rate used in the transaction and the exchange rate in the pertinent foreign country as of the close of business on the preceding day. The financial institution would also have to disclose all commissions and fees charged for the transaction. Such information would have to be posted on the premises, on all forms and receipts, and in any print, broadcast, or electronic advertisements when applicable.

11. Financial Information Privacy Act of 1999 (S. 187). Introduced by Senator Sarbanes (D-MD) on January 19, 1999.

Status: Referred to the Committee on Banking.

This bill would require the banking agencies to issue final rules that would oblige financial institutions to secure a customer's permission before releasing any confidential information about the customer. Specifically, financial institutions would be prohibited from sharing confidential data with an affiliate if the customer has forbidden such disclosure. In addition, financial institutions could not disclose private information to an outside source unless the customer consented to the disclosure. The institution would have to inform the customer of the nature of the information shared and under what circumstances the disclosure took place. Finally, customers would have to be given access to the confidential information so that they could review it for accuracy.

12. Consumer Debit Card Protection Act (H.R. 445). Introduced by Representative Barret (D-WI) on February 2, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Electronic Fund Transfer Act (EFTA) by adding consumer protections. The bill would differentiate between an ATM card and a check card for purposes of EFTA. An ATM card is any card that is issued by a financial institution for use in initiating electronic funds transfers from automated teller machines and other electronic terminals and which requires a unique form of identification (other than a signature), such as a PIN or a fingerprint. A check card is any card that can initiate an electronic funds transfer from a customer's account without the use of such an identifier. All check cards would have to have the term check card prominently displayed on its face.

When an issuer sends an unsolicited check card to a consumer, the card must not be activated without customer authorization. The issuer would also have to clearly state that once activated, the check card may be used without a code or unique identifier. An issuer sending a check card in response to a consumer's request for an ATM card must promptly issue an ATM card if the consumer refuses the check card.

The bill would also limit a consumer's liability for a fraudulent electronic funds transfer to $50 if the transfer was initiated by someone besides the consumer and the transfer did not require the use of a unique identifier, other than a signature. The consumer would not be liable for any losses if an unauthorized transfer took place after the card issuer had been notified that the account was in jeopardy.

In addition, financial institutions that issue check cards must provide a 24-hour toll-free number to which consumers can report missing or stolen cards. A charge for insufficient funds could not be assessed to a consumer if an unauthorized electronic funds transfer caused the insufficiency. A depository institution that receives notice from a consumer of an error regarding an electronic funds transfer must provisionally credit the consumer's account while it continues to carry out an investigation that must be completed within five days.

13. FinCen Public Accountability Act (H.R. 517). Introduced by Representative Paul (R-TX) on February 3, 1999.

Status: Referred to the Committee on Banking and Financial Services and the Committee on Government Reform.

This bill would require the Financial Crimes Enforcement Network (FinCen) to comply with established federal guidelines that cover the safeguarding and disclosure of information collected on individuals by government agencies. These guidelines include provisions that require: 1) FinCen to seek permission from the individual before releasing information about him/her; 2) the individual to be notified when information about him/her has been released; and 3) the individual be given access to information collected on him/her as well as an opportunity to make corrections to incorrect data. Under the bill, the Secretary of the Treasury would not be free to exempt FinCen from these guidelines.

FinCen was established in 1990, in part to support and strengthen domestic and international anti-money laundering efforts.

14. Bank Secrecy Sunset Act (H.R. 518). Introduced by Representative Paul (R-TX) on February 3, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend Title 31, Chapter 53, United States Code by repealing subchapters II and III of this chapter within one year of passage of the bill. The provisions to be repealed require domestic financial institutions involved in certain monetary transactions to file a report of the transaction. The provisions also require individuals involved in foreign transactions to keep records on the participants in the transactions and file a detailed report whenever an international monetary transaction over $10,000 is undertaken.

The bill would also repeal Chapter 12, Sec. 1951 of the United States Code, which requires certain financial companies to maintain business records that are useful in criminal, tax, or regulatory investigation proceedings.

Finally, this bill would disallow any current or future regulations issued by bank regulators to monitor the account of a financial institution's customer or to obtain information regarding a person involved in a financial transaction at a financial institution.

15. Cash Consumer Protection Act (H.R. 599). Introduced by Representative Fattah (D-PA) on February 4, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Consumer Credit Protection Act by making it illegal to refuse to sell or lease to a consumer because the consumer does not possess a credit card. It would also be illegal to demand an unreasonable cash deposit from a consumer not in possession of a credit card.

16. SAIF and DIF Reserve Fund Elimination Act (S. 377). Introduced by Senator Enzi (R-WY) on February 4, 1999. Related Bills: H.R. 687

Status: Referred to the Committee on Banking.

This bill would amend the Federal Deposit Insurance Act and the Deposit Insurance Funds Act of 1996 by eliminating the special reserve funds of both the Savings Association Insurance Fund and the Deposit Insurance Fund. These reserve funds were designed to provide emergency funding should the funds drop to dangerously low levels.

17. Community Development Financial Institutions Fund Amendments Act of 1999 (H.R. 629). Introduced by Representative Vento (D-MN) on February 8, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Community Development Banking and Financial Institutions Act of 1994 by establishing the Community Development Financial Institutions Fund (CDFIF) as a corporation under the authority of the Department of the Treasury. The CDFIF would provide funding for community development financial institutions (CDFIs).

The bill would make CDFIs eligible for community enterprise assessment credits given by the Community Enterprise Assessment Board. Assessment credits are used by insured depository institutions to offset the FDIC's semiannual insurance fund assessments. Assessment credits are currently based on the level of an institution's deposits that come from residents of a distressed community. Under this bill, credits would be based on the increase in these deposits at the institution for the respective period.

18. Federal Home Loan Bank System Modernization Act of 1999 (H.R. 822). Introduced by Representative Baker (R-LA) on February 24, 1999. Related Bills: S. 458.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Federal Home Loan Bank Act to make operational changes to the Federal Home Loan Banks (FHLBs) and to expand the membership of the Home Loan Bank System, which currently includes only qualified thrift lenders.

The Federal Home Loan Bank Board would be abolished, and the newly created Federal Home Loan Bank Finance Corporation (FHLBFC) would assume its duties. The FHLBFC would be managed by representatives from the Home Loan Banks and would have the sole right to issue voting capital stock and debt securities on their behalf.

The Home Loan Banks would be allowed to merge or reorganize under the directions and requirements put forth by the FHLBFC. Each Home Loan Bank would be able to modify the election and appointment procedures for its board of directors. The Home Loan Banks would also be able specify the contractual terms of advances to members without approval from the Federal Housing Finance Board.

The criteria for membership in the Home Loan Bank System would be significantly eased to permit any community financial institution (CFI) to join. Any financial institution with insured deposits and assets of under $500 million would qualify as a CFI. These institutions could receive advances to make small-business, agricultural, rural development, or low-income loans, in addition to residential housing loans, and would not need to hold a minimum percentage of assets in residential mortgage loans. Savings associations that do not qualify as a CFI must retain their qualified thrift status to maintain Home Loan Bank membership.

19. Bankruptcy Reform Act of 1999 (H.R. 833). Introduced by Representative Gekas (R-PA) on February 24, 1999.

Status: Referred to the Committee on Banking and Financial Services and the Committee on the Judiciary.

This bill would overhaul the United States Bankruptcy Code (11 U.S.C.). It is intended to end perceived abuses of the current bankruptcy system. These changes would become effective 180 days after the enactment of this bill. The major provisions that apply to the banking industry are summarized below.

Consumer Bankruptcies. Creditors and interested parties could ask the bankruptcy judge to convert a case from Chapter 7 (liquidation) to Chapter 13 (debt adjustment). The bill establishes a presumption that a debtor has used the bankruptcy courts abusively if the debtor has applied for Chapter 7 relief but has current monthly income, less expense allowances and payments on secured debts, greater than the $5000 or 25 percent of unsecured claims against the debtor, whichever is less. The bankruptcy trustee would also take into account whether the debtor has extraordinary expenses when deciding if the debtor has abused the right to file under Chapter 13. The trustee would then make a recommendation to the bankruptcy court, which would make the final judgment as to whether the case should be converted to Chapter 13 or dismissed. Dismissal of a case along with findings of improper actions by the debtor's attorney could result in civil damages to be paid by the debtor's attorney.

The bankruptcy court would be able to terminate the automatic stay on actions against the debtor's property if the court determines the debtor has been abusing the protection. Certain consumer debts, including those incurred to satisfy a nondischargeable debt, undertaken within the 90 days prior to filing would not be dischargeable. Leased items must be returned to the creditor within 30 days of filing, unless the creditor allows the debtor to assume the lease.

Debtors could not use Chapter 11 or Chapter 13 if they have received a bankruptcy discharge within the past eight or five years, respectively. A judge could not approve a plan under Chapter 11 or 13 that does not address the payment of outstanding domestic support obligations. These obligations would be assigned top priority on the list of unsecured claims against the debtor.

To be eligible for a discharge of debts, debtors would also be required to complete a financial management course after filing under Chapter 7 or Chapter 13.

Consumer Protections. The bill would protect consumers by requiring debt-relief agencies to supply consumers with certain information at the start of the relationship. Debt-relief agencies are for-profit persons or entities that provide bankruptcy assistance to a debtor. These agencies would need to supply information to the consumer on: 1) his or her options regarding legal representation; 2) the costs and types of services provided by the agency; 3) information on the different types of bankruptcy; and 4) fees and documents needed to proceed with a case. The agency would be required to show the debtor how to properly value assets and income and would have to explain the importance of supplying accurate information to the court. An agency that did not disclose this information, did not following the federal rules of bankruptcy procedure, or was responsible for the dismissal or conversion of a case because of improper filing of papers could be held liable to the debtor for civil damages.

The creditor would need to make the debtor aware of their right to a bankruptcy hearing before reaffirming an unsecured debt. At the hearing, the judge would make a ruling as to whether the affirmation was in the best interest of the debtor. Creditors using the courts to unduly coerce a reaffirmation of a debt from a debtor could be held liable for expenses incurred by the debtor in fighting the reaffirmation. A debtor could have his or her claims reduced 20 percent if the debtor shows that the creditor refused to negotiate an alternative payment schedule put forth by an approved credit counseling agency in the 60 days prior to filing.

International Bankruptcies. This bill would create Chapter 15 of Title 11 to manage cross-border bankruptcies. This chapter would expand the scope of bankruptcy law to incorporate the model law on cross-border insolvency. It would establish a statutory mechanism to address cross-border insolvencies and to facilitate cooperation between the trustees, and debtors in the United States, and their foreign counterparts.

Financial Contracts. The bill would amend the bankruptcy code and the Federal Deposit Insurance Act to clarify the treatment of various derivative contracts when a counterparty becomes insolvent. For the most part, such agreements are exempted from the automatic stay and remain apart from the property of an estate.

The bill recognizes master agreements between counterparties as contracts exempted from the automatic stay. Such agreements govern netting arrangements across a number of contracts between counterparties.

The bill also clarifies conditions in which walkaway clauses in financial contracts with depository institutions in default could not be exercised.

20. Credit Card Consumer Protection Act of 1999 (S. 480). Introduced by Senator Schumer (D-NY) on February 25, 1999. Related Bills: H.R. 900, H.R. 1276

Status: Referred to the Committee on Banking.

This bill would amend the Truth in Lending Act (TILA) by adding requirements and consumer protections regarding the use of credit cards. Under the bill, a consumer could not be assessed any fee solely for paying balances before interest accrues, although annual membership fees would not be prohibited. A card issuer would have to give a consumer at least 15 days prior notice of an increase in the rate of interest. A consumer who decides to cancel his or her account would be permitted to make payments on existing balances at the rate prevailing prior to the increase.

The bill would also require creditors to prominently disclose to the consumer the amount of transaction fees, percentage rates, and finance charges related to the use of third-party checks. Creditors would be barred from imposing fees on consumers who exceed their credit limits if the creditor approved the transaction. A creditor offering a plan without finance charges for an introductory period would be barred from assessing a finance charge on the balance incurred prior to the end of the introductory period. Finally, card issuers offering introductory rates would also be required to disclose the rates that would take effect at the end of the introductory offer.

21. Consumer Credit Report Accuracy and Privacy Act of 1999 (H.R. 1015). Introduced by Representative Roybal-Allard (D-CA) on March 4, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Fair Credit Reporting Act to require each credit-reporting agency to supply one free credit report annually, if a consumer requests a report.

22. Consumer Lease Protection Act (H.R. 1332). Introduced by Representative LaFalce on March 25, 1999.

Status: Referred to the Committee on Banking and Financial Services.

This bill would amend the Truth in Lending Act (TILA) by raising the dollar level of transactions that are exempt from disclosure requirements. Currently, credit transactions and lease transactions over $25,000 are exempt from disclosure requirements. The bill would make transactions over $50,000 exempt from disclosure requirements.

The Consumer Credit Protection Act would be amended to make creditors who do not comply with disclosure requirements subject to civil penalties. The upper limit on class action liabilities would be raised to $1 million or 1 percent of the creditors' net worth, whichever is less.

SUMMARY OF FEDERAL REGULATIONS

Board of Governors of the Federal Reserve System

Check Processing (2/24/99)
Gave notice of proposed rulemaking that would give banks the option of sending “notice of dishonor” or “notice of nonpayment” electronic statements to each other instead of returning the original checks. Current Board regulation requires paying or returning banks to return either the original check, a front and back copy of the check, or, in special circumstances, written notice containing specific check information. Comments were due April 30, 1999. For further information, see 64 *Federal Register*, pp. 9105-7. (Regulation CC)

Electronic Funds Availability (3/26/99)
Issued a final rule to give banks more time to implement merger-related software changes. Banks that consummate a merger between July 1, 1998, and March 1, 2000, would be treated as separate banks, with regard to Regulation CC’s merger provisions, until June 1, 2000. Merger consummations that take place after March 1, 2000, would have the standard one-year transition period in which to implement software changes. This rule became effective April 1, 1999. For further information, see 64 *Federal Register*, pp. 14577-8. (Regulation CC).

Federal Deposit Insurance Corporation

Risk-Based Capital (3/2/99)
Together with the Federal Reserve Board, Office of the Comptroller of the Currency, and Office of Thrift Supervision issued a final rule that would make the agencies' regulations uniform in the following four areas: 1) construction loans on pre-sold residential properties; 2) junior liens on 1- to 4-family residential properties; 3) investments in mutual funds; and 4) Tier 1 leverage ratio.

Qualifying residential construction loans are eligible for a risk weight of 50 percent. Previously, OCC and OTS rules allowed these loans to be eligible for a 50 percent risk weight only if the property was sold before the bank made the loan to the builder.

To determine the loan to value (LTV) ratio and capital requirements, a bank holding multiple liens on a 1- to 4-family home will be viewed as having a single extension of credit secured by the primary lien, provided the bank is the sole holder of all liens on the property. The combined loan amount will be assigned to either the 50 or 100 percent risk category. Eligibility for the 50 percent risk category would depend on the underwriting standards of the loan, LTV ratio, and repayment status of all the loans.

Institutions would have two options for assigning risk weights to investments in mutual funds. First, an institution's total investment in a mutual fund could be assigned the risk category corresponding to the highest risk-weighted asset capable of being held by the fund according to its prospectus or the institution could assign risk levels to the investment based proportionately on the investment limits in the fund's prospectus. Regardless of which method is used, the minimum risk weight for any mutual fund investment is 20 percent.

To receive the highest rating under the Uniform Financial Institutions Rating System, financial institutions must have a minimum Tier 1 leverage ratio of 3.0 percent. All other institutions must maintain a minimum ratio of 4.0 percent. A Tier 1 leverage ratio is the ratio of Tier 1 capital to total assets. It serves as an indicator of the institution's capital adequacy. This rule became effective April 1, 1999. For further information, see 64 *Federal Register,* pp. 10194-201. (Regulation H)

Know Your Customer (3/29/99)
Withdrew from further consideration the proposed "know your customer" rule. The proposed rule would have required financial institutions to: 1) determine its customers' identity and source of funds; 2) determine what are normal transactions for each customer; 3) monitor the account for transactions that fall outside this norm; and 4) in accordance with the agency's regulations on reporting suspicious activity, report these suspicious transactions to the FDIC. The proposal, which had been made in cooperation with the other federal banking agencies, met with significant opposition from legislators, citizens, and financial institutions. For further information, see 64 *Federal Register,* p. 14845.

Office of Thrift Supervision

Capital Distributions (1/19/99)
Issued a final rule exempting some institutions from filing an application or notice before making a capital distribution. To be exempt from filing, an institution would have to remain well capitalized after the distribution and could not be a subsidiary of a savings and loan holding company. The distribution could not be used to retire any part of the institution's common stock, preferred stock, or debt instruments. Also, the amount of all capital distributions made in a single year could not exceed the institution's net income for that year to date plus the institution's retained earnings for the previous two years. Other provisions streamline the application procedures and make technical changes to the definition of a capital distribution. This rule became effective April 1, 1999. For further information see, 64 *Federal Register,* pp. 2805-10.

Savings and Loan Holding Companies (2/8/99)
Gave notice of proposed rulemaking that would treat multiple savings and loan holding companies that make supervisory acquisitions as unitary thrift holding companies. Supervisory acquisitions are those authorized by the Federal Deposit Insurance Corporation (FDIC) for the purpose of rescuing a financially troubled savings association. Holding companies would be viewed as unitary thrifts if: (1) the holding company controls more than one savings association after a supervisory acquisition and the acquired association continues to exist as an identifiable savings association subsidiary; or (2) the holding company controls a particular savings association after a supervisory acquisition and later acquires an additional association as a separate subsidiary. Comments were due April 9, 1999. For further information, see 64 *Federal Register,* pp. 5982-5.

On February 5, 1999, the Alabama Court of Civil Appeals upheld a lower court ruling that credit protection products are not insurance products and so are not subject to regulation by the state. The case *(Steele v. First Deposit National Bank, Ala. Ct. Civ. App., No. CV-96-6965, 2/5/99)* was brought by Vola G. Steele, who alleged that by offering credit protection products, the banks were engaged in insurance activities, which would have been a violation of Alabama law. Credit protection products are arrangements between a bank and its customer that allows the customer to freeze his/her payment obligation to the bank. The protection does not cancel debts.

The initial trial court found that these products were not insurance products. The Court of Civil Appeals, referring to a United States Supreme Court test for insurance, agreed. Credit protection does not have the effect of transferring or spreading risk, nor is it limited to parties within the insurance industry. In addition, it does not constitute an integral part of the policy between a bank and a borrower. Therefore, banks that offer credit protection products are regulated by the National Bank Act and are not subject to Alabama's insurance laws.

The California Supreme Court, on February 24, 1999, chose not to review a lower court ruling that blocked Bank of America's attempt to impose binding arbitration on its credit card customers. The court's decision (*Badie v. Bank of America, Calif., No. S055552, 2/24/99*) validates the ruling of the Court of Appeals for the First District of San Francisco (November 4, 1998) that the "change of terms" clause, as written in BofA's account agreement, did not give the bank the right to deny its customers their right to a jury trial. Bank of America has indicated that it would not pursue the case. [See *Banking Legislation and Policy*, Fourth Quarter 1998, for a summary of the case.]

New Jersey
On January 7, 1999, senators Kavanaugh (R) and Bucco (R) introduced S. 1611. The bill would authorize the banking and insurance commissioner to set the maximum checking overdraft fee a state-chartered depository institution could charge a customer. The bill would also require depository institutions to disclose their fee schedules for transactions. Customers would also have the option of not proceeding with a transaction if they objected to the fee. Fees charged to a customer because the customer used a service of the bank in person would be prohibited. Automated teller machine (ATM) fees would be frozen until the commissioner concludes an investigation into fee practices at ATM machines.

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