Leach Keynote Address

James A. Leach*
CONGRESSMAN LEACH: Thank you Dean Feerick, Secretary Carnell and Laurie Schaffer. Many of you do not know Ms. Schaffer, but she is a staff member of the Banking Committee and a graduate of Fordham Law School. I would like to briefly recall one of my proudest moments working with Ms. Schaffer. We had worked on a little bill for a few years, and the final draft came out to be over 400 pages. One night we called representatives of the U.S. Treasury and the U.S. Federal Reserve Board into a room, each having a dozen lawyers, and for eight hours reviewed the final text. At the end of this review, they found one typographical error. I was very proud of that. I mentioned that to Federal Reserve Chairman Alan Greenspan, and he said, “One?”

I am also proud to be at a school where the Associate Dean is Michael Martin. I don’t know if any of you have taken a course taught by Professor Martin, but you should know that he has one of the most stellar academic backgrounds that anyone could have. He is a fellow graduate of the Davenport High School in Davenport, Iowa.

In any regard, it strikes me that the fundamental challenge of Congress in financial services has been to try to come up with a framework for our times. We like to use the analogy “bridge of the century” or “the millennium,” but basically the framework is for our times. What happened in financial services is that the market got well ahead of the law. So the effort has been (a) to

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1. Cameron Professor of Law and former Associate Dean at Fordham University School of Law. See generally, http://law.fordham.edu/homejump.ihtml?pageid=165 (last visited September 18, 2000).
catch up with the market and (b) to pass a law that could be flexible and adapt to future developments.

Some background: in 1933 the U.S. Congress passed a law, called the Glass-Steagall Act,¹ which had the effect of separating commercial and investment banking. It was passed under the assumption that, as the Great Depression hit and many people lost money, conflicts of interest had developed and some people on Wall Street had advantages over the general public.³ Actually, later reviews of this assumption found it to be somewhat frail.⁴ In retrospect, it seems that more people were jumping out of buildings on Wall Street than most places in America and that Glass-Steagall was rooted more in resentment than in need.

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³ See Susan M. Golden, Symposium on Securities Market Regulation: Probing the Limits of National Bank Powers under the Glass-Steagall Act, 36 CATH. U.L. REV. 1025 (1987) (“[The Glass-Steagall Act] was intended to restore public confidence in banking, to ensure and maintain the economic stability of banks by prohibiting unsound and imprudent bank investments, and to prevent potential conflicts of interest between commercial and investment banks.”); Joseph Michael Heppt, Note, An Alternative to Throwing Stones: A Proposal for the Reform of Glass Steagall, 52 BROOK. L. REV. 281, 289 (“Congress also sought to prevent the conflicts of interest that arose when commercial bankers engaged in securities activities. . . A banker faced with a faltering securities offering that his bank had underwritten may have advised his banking customers to purchase the securities, thereby saving the securities offering and making a commission on the sale as well.”).

⁴ See Susan Sirota Gaetano, Note, An Overview of Financial Services Reform 1988, 5 CONN. INS. L. J. 793, 797-798 (1999) (“Studies show that banks that engaged in stock market investment before the Glass-Steagall Act was enacted were less likely to fail than those that were not involved in investment activities.”).
Even if Glass-Steagall had a certain validity in the 1930s, the market shifted somewhat gradually until the late 1980s and 1990s, when it shifted on a quantum basis almost every four or five years. Customers came to prefer and use new and more sophisticated products that, particularly in the banking industry, made many traditional banks irrelevant to their customers. For example, over a thirty-year period, traditional banks went from holding about two-thirds of the saved dollar in America to holding about one-quarter of the saved dollar in America.\(^5\) Banking was truly on a trend that might be described as “in eclipse,” but even this is an understatement.

This is a very difficult area in which to legislate in because there are differences between and within various industrial sectors, as well as between and within regulatory branches and levels of government. It is also a difficult area to legislate because, in the end, a legislative body is a public body and it is the public interest that comes first. This concept of the public interest must be kept at the forefront — not the concerns of any particular industrial arrangement.

In creating financial services legislation, there were also problems concerning timing and control. Even though the public interest was the main concern, particularly to me as Chairman, it was quite clear that various parts of the financial sector had virtual vetoes over other parts.\(^6\) As the legislative process developed, timing became an extraordinary problem. Some particular institutions within industrial groupings had theoretical support for broad approaches. They were, however, very concerned that other institutions had a “leg-up” and that these institutions would be able to take advantage of a situation faster and more comprehensively

\(^5\) See, e.g., Finance Service Restructuring: Hearing Before the Comm. on Banking and Fin. Serv., 105th Cong. 22-23 (1997) (statement of William T. McConnell, President, Am. Bankers Assoc.) (“Under the current regulatory regime, banks have lost traditional market share to other financial service providers. In fact, while the assets banks hold have increased, banks' market share of total assets has fallen steadily over the past two decades.”).

\(^6\) See Dean Anason, Financial Firms Try to Tweak Reform Law to Gain Powers, AM. BANKER, Feb. 23, 2000, at 1 (stating that numerous firms sought to use their lobbying powers to obtain a veto for new financial services legislation).
than they could. So there was a great deal of concern over the minutiae, sometimes because detail mattered, other times because stalling appeared to be in the vested interest of one particular company or kind of company vis-à-vis another.

The legislative approach we took was that of a three-way street. That is, banks were given securities and insurance powers. Insurance companies were given banking and securities powers and securities companies were given banking and insurance powers. The approach taken was a very competitive approach that I believe is good for consumers and America’s financial position in the world.

From the consumer perspective, the Department of Treasury estimates that there will be a savings of about $18 billion a year. There will be advantages in single-shop banking or financial servicing. There will be new privacy protections. This legislation contains the greatest privacy protections ever passed in a modern-day statute. For example, there is a prohibition on disclosure of account numbers to third-party telemarketers. There is also a

7. See, e.g., Clyde Mitchell, Financial Modernization - One Year Later, N.Y. L.J., Jan. 19, 2001, at 3 (referring to “the ‘turf warfare’ among the banking, securities and insurance industries that existed prior to [Gramm-Leach-Bliley]”).

8. Gramm-Leach-Bliley Financial Services Modernization Act, Pub. L. No. 106-102, § 103(a), 113 Stat. 1338 (declaring that financial holding companies may have the ability to “[i]nsure . . . against loss, harm, damage, illness, disability, or death” and may also “[u]nderwrite, deal[ ] in, or mak[e] a market in securities”).


10. See Gramm-Leach-Bliley Financial Services Modernization Act § 103(a) (authorizing securities firms to engage in banking and insurance functions that they had previously been barred from).


12. See Gramm-Leach-Bliley Financial Services Modernization Act §§ 501-510 (regulating disclosure of nonpublic personal information by banks, insurance companies, and securities firms); id. §§ 521-527 (regulating fraudulent access to financial information by banks, insurance companies, and securities firms).

13. Id. § 502(d) (“A financial institution shall not disclose, other than to a
In addition — and I throw this out to those of you who are about to become active lawyers — there is potential liability for lawyers here, liability that would put some lawyers in America today behind bars for a very subtle act. In this world, where people want information about everyone else, there is a growing use of privatized and private investigative agencies to find information about competitors for clients. One of the things that is now almost universally done in the private investigation industry is what is described as “pretext calling” or “pretext identity theft.” This is where an individual might call up a bank and say, “I’m Joe Smith, I want to know what’s in my bank account.” Lawyers are involved because they hire these firms. We are now making this a crime, one that is subject to both civil and criminal penalties.

This is something that is not of light import. We received a great deal of testimony in the House Banking Committee on how

consumer reporting agency, an account number or similar form of access number or access code for a credit card account, deposit account, or transaction account of a consumer to any nonaffiliated third part for use in telemarketing, direct mail marketing, or other marketing through electronic mail to the consumer.”)

14. Id. § 502(b) (pointing out that a financial institution may not disclose non-public information about its customers to non-affiliated third parties unless the consumer is made aware that such disclosure may and possibly could occur and “is given the opportunity... to direct that such information not be [so] disclosed”).

15. Id. § 503 (providing that financial institutions must provide consumers with the institution’s policies and practices on consumers privacy on a yearly basis).

16. Financial Information Privacy Act: Hearing before the House Comm. on Banking and Fin. Serv., 105th Cong. 73 (1998) (statement of Rep. James Leach) [hereinafter Leach Statement] (stating before the House Banking and Financial Services Committee that in “[r]ecent years [there has been] a proliferation of business enterprises that specialize in the collection and dissemination of personal financial information... who market their services to law firms... seeking to obtain information of a public and nonpublic nature”).

17. Gramm-Leach-Bliley Financial Services Modernization Act § 523 (mandating fines and/or imprisonment for up to five years for violation of the legislation's pretext calling provisions).
pervasive this kind of practice has become.\textsuperscript{18} The legal profession must be alerted to it. One of the examples of pretext calling's widespread use is the extraordinary amount of advertisements for investigative services that specialize in this area that appear in virtually all law journals and various legal publications. That is a fair indication of how widespread it has become.

With regard to the consumer provisions — and there is always the question of whether to go further — I stress (a) that they are more comprehensive than people know, (b) that they will become stronger, even without new legislation, and (c) that they are a little wider than some industrial sectors currently understand. Let me explain - the way the privacy provisions work is that if something is financial in nature, such as the issue of travel services, a bank will have the privacy provisions in its travel services subsidiary come under the privacy protections of the new legislation. In addition, all other travel agents in America will also come under the same privacy provisions. Many travel agents are unaware that these provisions apply to them.

In addition, the new legislation has a provision that is designed to be more flexible in order to remain relevant in the future financial world. For example, under the old Bank Holding Company Act,\textsuperscript{19} a bank could do things that were "banking in nature," largely as adjudicated or assessed by the Comptroller,\textsuperscript{20}

\textsuperscript{18} See Leach Statement, supra note 16.


\textsuperscript{20} Office of the Comptroller of the Currency (the "OCC"). The OCC is an independent bureau of the Department of the Treasury. It charters, regulates,
but also potentially by the Federal Reserve Board. Under the new law, banks can do things that are "financial in nature," and that is a broader definition than "banking in nature." As each of these new functions that might be described as "financial in nature" comes into being, they come under the privacy protections of the law — and so does the whole private sector that might be involved in it. Here is an exaggerated example: if the Federal Reserve Board declared that funeral services were financial in nature, that would mean that any funeral services information that a bank would have would come under the privacy protections. But, in addition, the entire American funeral services industry would be brought under the privacy protections of the Act. So these provisions get broader with time, rather than narrower.

In terms of being good for America's competitiveness in the world, one of the interesting aspects of American finance in the three areas of securities, commercial banking, and insurance is that around the world various companies have different beachheads. In one country, Citigroup might be very important. In another country, Prudential Insurance might be important, and in another country, Goldman Sachs might be important. By allowing each of these American companies to offer a wider variety of products, I think we are going to see America's position in financial services become much stronger. This is important because some of our European competitors have broader rights; but it is also important in and of itself.

Here I would like to mention, with some concern, what the

and supervises all national banks. The OCC also supervises the federal branches and agencies of foreign banks and serves as one of the directors of the Federal Deposit Insurance Corporation ("FDIC"). See http://www.occ.treas.gov/AboutOCC.htm (last visited Oct. 20, 2000).


22. See id. § 509; see also Paul J. Polking & Scott A. Cammarn, Overview of the Gramm-Leach-Bliley Act, 4 N.C. BANKING INST. 1, 27 ("Because extending credit is a financial activity described in Section 4(k) [of the Bank Holding Company Act], a retailer that provides open-end credit accounts or sales finance to its customers will be a 'financial institution' and subject to the privacy provisions in Title V."
bill\textsuperscript{23} does not do. While it opens up the financial industry to all kinds of new competition, it forestalls the formal mixing of commerce and banking. Indeed, it closes the one loophole in the current law, which is called the "unitary thrift loophole."\textsuperscript{24} Let me stress this distinction and what the law does and does not do.

The aim of this law is to have terrific open-ended competition within financial services. It also looks, however, towards making financial services into an independent area of American commerce. For example, you can have a unity, as you see in the Citigroup model, of an insurance company, a securities firm, and a banking firm. You cannot, however, have, under this law, Citigroup merging with General Motors or with Wal-Mart.

We have some history in this country of a merging of commerce and banking, particularly in the 19th century.\textsuperscript{25} We also have more modern-day mergers of commerce and banking around the world, especially in parts of Europe, and certainly in Japan.\textsuperscript{26} The United States does not allow these types of mergers, however, partly because of the social safety net included with deposit insurance.\textsuperscript{27} If you applied deposit insurance to banks, which surely

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\item \textsuperscript{24} See id. § 401; see also Polking & Cammarn, supra note 22, at 26 (stating that from the view of these two authors that the Gramm-Leach-Bliley Financial Services Modernization Act "prohibits the formation of unitary thrift holding companies").
\item \textsuperscript{26} See \textit{Financial Services Modernization Act: Hearing before the House Comm. on Banking and Fin. Serv.}, 106th Cong. 2 (1999) (statement of David H. Komansky, Chairman and Chief Executive Officer of Merrill Lynch & Co., also called Merrill Lynch Pierce Fenner and Smith, Co.) ("Europe has long allowed its financial houses to offer banking, securities, and insurance services. And even Japan reformed its version of Glass-Steagall.").
\item \textsuperscript{27} See 12 U.S.C. § 1821(a)(1)(B) (2000) (limiting FDIC protection to $100,000). See generally Mark E. Van Der Weide and Satish M. Kini, \textit{Subordinated Debt: A Capital Markets Approach to Bank Regulation}, 41 B.C. L. REV. 195, 204 (2000) [hereinafter Weide & Kini] (identifying and explaining that there are three main elements of the banking safety net, which are "(1) federal insurance of banks' deposits for up to $100,000; (2) access for banks to emergency cash through the Federal Reserve's discount window; and (3) access for banks to the Federal Reserve's payment system").
\end{itemize}
are associated with commercial concerns, one question is whether that deposit safety net gets spread too wide, leading to greater public liability.

We have found in Europe that this is the case. The French taxpayers and the Spanish taxpayers have forked out billions of francs and pesetas, respectively. Arguably, it is one of the principal problems in the Japanese economy. In my view, there is no economic case whatsoever for applying the economies of scale argument to merging commerce and banking, in most instances, and there is certainly no national interest in doing so. I stress this point for a number of reasons. One, because the U.S. Treasury initially strongly pushed for new legislation, as did other powerful interests in the American economy and some very important members of Congress. The Federal Reserve itself originally supported a modest basket approach (the basket approach being the authorization of a commercial bank to have five or ten or fifteen percent of its assets in commercial endeavors). But upon

28. See Banesto Fiasco, ECONOMIST, Jan. 8, 1994, at 19 (reporting on the collapse of Spain’s fourth-largest bank and the subsequent intervention of the Spanish government with funds to prevent the collapse of said bank); see also Credit Lyonnais: Humbled, ECONOMIST, Mar. 26, 1994, at 96 (reporting on Credit Lyonnais’s massive losses and subsequent bailout by the French government, again to prevent the collapse of said bank).

29. See, e.g., Mark Tran, American Notebook: New Life is Breathed into Banking Reform, GUARDIAN (London), May 13, 1991 (discussing the “ambitious elements of the Treasury plan that would allow bank affiliates to enter the securities and insurance business[...] limit the coverage of the deposit insurance system and allow commercial companies to own banks”).

30. See e.g., Financial Services Modernization Act: Hearing before the House Comm. on Banking and Fin. Serv., 106th Cong. 2 (1999) (statement of John B. McCoy, President and Chief Executive Officer of Banc One Corp.) (stating that “[Banc One officials] are confident that the proposals that Congress has considered to mix banking and commerce could be safely and soundly executed by this Nation’s financial services and companies and commercial firms”).

31. See Jayne Levin, Banking Reform Jello; Structural Changes This Year Unlikely, 1991 INV. DEALERS’ DIG., Mar. 4, 1991 (“The measures by [former member of the House Banking Committee United States Representative (Democrat-Georgia) Doug] Barnard and [former member of the House Banking Committee Unites States Representative (Republican-Ohio) Chalmers] Wylie seek to encourage outside sources of capital to strengthen commercial banks.”).

32. See, e.g., Hearing of the Financial Institutions and Consumer Credit
review of even that modest plan, it became evident that we would no longer have an independent financial sector.

I stress this one point very strongly, that if you passed the authorization for commerce and banking to be merged, there would be no independent major financial institution in the United States. That is, within months, Citigroup would be taken over by AOL/Time Warner, General Electric, or perhaps Microsoft. For example, if you look at the valuations at a market level of the new kinds of companies, it is impressive. Only one of our financial companies is in the top twenty. Virtually every financial institution would be a major takeover target. Those that had advocated merging commerce and banking did so thinking that banks would be the acquirers. Actually, they would likely become the acquired.

It is my own personal sense that if you ask what is different in the American economy from thirty or forty years ago — and there are hundreds.

One of the differences that can be pointed out — is that we have developed a new capacity, symbolized by New York in some ways, to leverage capital and come to control institutions of one kind or another through such leverage. But there is a great difference between the ability to leverage capital and do mergers and acquisitions on the one hand, and the ability to manage companies on the other. I will tell you that the idea that America would be better off taking x-number of companies from the New York Stock Exchange and shrinking it ten-fold is not clear-cut to me and is one about which we should be very concerned.

I stress this whole issue because this commerce-and-banking circumstance can spring up without warning unless we are extraordinarily vigilant. However, I believe that the “keiretsu-
sization\textsuperscript{34} of our economy, the concentration of ownership, is not the American way. You will find political, as well as economic, backlash to such a principle, which I think is more rooted in hubris than it is in the national interest.

Finally, a note about regulation and process itself. Part of the legislation is simply about regulation.\textsuperscript{35} One of the great surprises in the development of the statute was that, just as there are rivalries which are well understood between industries and between big and the small companies, there ended up being significant rivalries concerning regulation. The private sector from time to time is hallmarked by maximization of profit motives, while the public sector sometimes by maximization of power. So we had a "battle royale," for example, between the Treasury Department and the Federal Reserve.\textsuperscript{35} This was partially reflected in the commerce and banking area.

It was my view - and I sometimes do not have a close-up view of some circumstances - that the Treasury's position was to vest more authority in the Treasury Department itself. At the same time, however, if you mixed commerce and banking, it would have put the Treasury at the forefront in American society for review of a huge amount of the American industrial base. This would have been very difficult in a governmental sense and would have resulted in a very politicized circumstance. For example, the Treasury would become the focal point for fund-raising in American politics. I think this would have been a major mistake, and a particularly advantageous one for incumbent administrations.

\textsuperscript{34} See Kai Schadbach, The Benefits of Comparative Law: A Continental European View, 16 B.U. INT'L LJ. 331, 410 (1993) (defining keiretsu as "the Japanese system of cross-shareholding between related corporations, both vertically and horizontally, with a core bank that advances relationships between the members").


\textsuperscript{36} Stephen Labaton, Deal on Bank Bill Was Helped Along by Midnight Talks, N.Y. TIMES, Oct. 24, 1990, at A1 (noting that one obstacle to the passage of Gramm-Leach-Bliley "was a turf battle between the Treasury [Department] and the Federal Reserve").
The compromise that was worked out in the end was unexpected. It was a compromise that was not necessarily appreciated by the Comptroller's Office, which is a division of the Department of Treasury, because the Federal Reserve got more or less independent protection. The balance though is one of good, solid competition where banks can choose between being regulated by the Federal Reserve or the Comptroller. The Treasury, however, got a somewhat greater political role, which I thought was very appropriate at the Secretary level. So there was a little bit of rivalry, not only between branches of government, but within one institution of government. That is, rivalry between the Secretary of the Treasury and the Comptroller's Office, which is a division of the Treasury itself. The final product puts the Secretary of the Treasury as a co-equal with the Chairman of the Federal Reserve in certain rule-making situations. This puts the constitutional role of the Executive Branch in play in, I think, an appropriate way, but it also protects the Federal Reserve itself as a regulator.

On the American political system, the way I look at it is that our country has never led the world more than it does today. We are the leaders in almost every area — from the arts to science to business organization. In politics, we are the great exception in terms of the quality of individuals serving in government. I think there are problems at virtually every level of government in terms of excellence. On the other hand, our political process is extraordinary. That is, the American political system is so strong

38. See Gramm-Leach-Bliley Financial Services Modernization Act, Pub. L. No. 106-102, § 721, 113 Stat. 1338; see also Weide and Kini, supra note 27, at 246 (explaining that there could be a problem with the division of authority because the "division of authority [between the Federal Reserve Board and the Department of Treasury regulators of the United States] allows banking firms to choose to structure their operations so that they fall within the purview of the regulator that the organization believes may be the most accommodating" thereby possibly circumventing the goals of Congress).
39. See id. §103(a) (requiring notification and consultation, among other things, between the Federal Reserve Board and the Secretary of the Treasury of the United States concerning "determination[s] of whether an activity is financial in nature or incidental to a financial activity").
that average people can do reasonably well within its parameters. Therefore, "process" in many ways is our most important political product.

As Chairman of the Conference Committee on this legislation,\textsuperscript{40} I insisted that we adopt a bipartisan and bi-institutional approach, as it would not have done much good to have a partisan product that would have been vetoed or a radical product that subsequent Congresses would have reformed. It was also extraordinarily important, at all stages in the process, to keep the public interest in mind. Issues of antitrust, privacy and consumer convenience, not institutional advantage, were the basic guideposts.

Making laws is, in the end, a confluence of three factors: substance, timing, and chemistry. The stars came into alignment for reform last year, but there should be little doubt that there is no inevitability to legislation of this kind. Differences within and between industries, rivalries within and between branches of government, House/Senate philosophical chasms, and a lack of goodwill in the American political process or system could all have derailed reform efforts at any point. The fact that the glue held together was rather remarkable. We now have a new dawn in financial services. I look forward to seeing how well our economy functions because of it.

Thank you very much.

Notes & Observations