STUDY & RECOMMENDATIONS REGARDING CONCENTRATION LIMITS ON LARGE FINANCIAL COMPANIES

FINANCIAL STABILITY OVERSIGHT COUNCIL

Completed pursuant to section 622 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

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CONTENTS

INTRODUCTION

Section 622 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act" or "Dodd-Frank Act") establishes a financial sector concentration limit that generally prohibits a financial company from merging or consolidating with, or acquiring, another company if the resulting company's consolidated liabilities would exceed 10 percent of the aggregate consolidated liabilities of all financial companies.[1] This concentration limit is intended, along with a number of other provisions in the Dodd-Frank Act, to promote financial stability and address the perception that large financial institutions are "too big to fail". Section 622 of the Act also requires the Financial Stability Oversight Council (the "Council") to: (i) complete a study of the extent to which the concentration limit would affect financial stability, moral hazard in the financial system, the efficiency and competitiveness of United States financial firms and financial markets, and the cost and availability of credit and other financial services to households and businesses in the United States; and (ii) make recommendations regarding any modifications to the concentration limit that the Council determines would more effectively implement section 622.[2] The Act requires the Council to complete its study and make its recommendations by January 21, 2011.

The Act specifically provides that the concentration limit set forth in section 622 is "subject to," and thus may be modified by, the recommendations made by the Council.[3] The Board of Governors of the Federal Reserve System (the "Board") is thus required to adopt regulations that reflect and are in accordance with the Council's recommendations to implement section 622.[4] The Board must prescribe these rules no later than 9 months after completion of the Council's study. The Board also is authorized to issue interpretations or guidance regarding application of the concentration limit to an individual financial company or financial companies generally.

This report fulfills each of these two Congressional directives to the Council in section 622. Part A provides a general summary of section 622's statutory provisions. Part B provides an overview of the effects of the concentration limit and discusses the specific effect of the concentration limit in the four areas that section 622 directs the Council to study and address. Part C briefly discusses several practical implementation issues that are raised by those provisions and contains the Council's three recommendations regarding modifications to the concentration limit that the Council has determined would more effectively implement section 622. The Council will request comment on the recommendations for a period of 30 days after publication in the Federal Register. The Council will review and, if appropriate, revise these recommendations in light of the comments it receives.

[1] Pub. L. No. 111-203, 124 Stat. 1376 (2010). In this report, we refer to the limit established by section 622 generally as the "concentration limit." This concentration limit was adopted as a new section 14 to the Bank Holding Company Act of 1956 (the "BHC Act") (to be codified at 12 U.S.C. § 1852) and, accordingly, terms used in section 622 have the meanings, if any, ascribed to them in the BHC Act unless otherwise provided.

[2] See 12 U.S.C. § 1852(e).

[3] See 12 U.S.C. § 1852(b).

[4] See 12 U.S.C. § 1852(d).

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

The Council believes that the concentration limit will have a positive impact on U.S. financial stability. Specifically, the Council believes that the concentration limit will reduce the risks to U.S. financial stability created by increased concentration arising from mergers, consolidations or acquisitions involving the largest U.S. financial companies. Restrictions on future growth by acquisition of the largest financial companies ultimately will prevent acquisitions that could make these firms harder for their officers and directors to manage, for the financial markets to understand and discipline, and for regulators to supervise. The concentration limit, as structured, could also have the beneficial effect of causing the largest financial companies to either shed risk or raise capital to reduce their liabilities so as to permit additional acquisitions under the concentration limit. Such actions, other things equal, would tend to reduce the chance that the firm would fail. Moreover, the concentration limit should provide a more comprehensive limitation on growth by acquisition than the 10 percent nationwide deposit cap imposed by the Riegle-Neal Act because it also takes into account non-deposit liabilities and off-balance sheet exposures, limiting incentives to shift liabilities from deposits to potentially more volatile on- and off-balance-sheet liabilities.

Although the Council expects the impact of the concentration limit on moral hazard, competition, and the availability of credit in the U.S. financial system to be generally neutral over the short- to medium-term, over the long run the Council expects the concentration limit to enhance the competitiveness of U.S. financial markets by preventing the increased dominance of those markets by a very small number of firms.

To more effectively implement section 622, the Council recommends: (i) modifying the statutory definition of "liabilities" for certain companies that do not currently calculate or report risk-weighted assets; (ii) modifying the calculation of aggregate financial sector liabilities to use a two-year rolling average instead of a single year for purposes of calculating the denominator of the limit and requiring the Board to publicly report, on an annual basis and no later than July 1 of any calendar year, a final calculation of the aggregate consolidated liabilities of all financial companies as of the end of the preceding calendar year; and (iii) extending the exception provided in the statute for the acquisition of failing banks to other failing insured depository institutions.

PART A: SUMMARY OF SECTION 622, AS ENACTED

The concentration limit established by section 622 has four principal components: (i) its general prohibition; (ii) the scope of financial companies to which it applies; (iii) the manner in which a financial company's liabilities are calculated for purposes of the concentration limit; and (iv) exceptions for certain types of transactions. Each of these components is described in further detail below.

1. GENERAL PROHIBITION

The concentration limit under section 622 prohibits any financial company from merging or consolidating with, acquiring all or substantially all of the assets of, or otherwise acquiring control of, another company if the total consolidated liabilities of the acquiring financial company upon consummation of the transaction would exceed 10 percent of the aggregate consolidated liabilities of all financial companies at the end of the calendar year preceding the transaction.[5] By its terms, the concentration limit applies to the acquisition by a financial company of any type of company, and is not limited solely to acquisitions of other financial companies. The concentration limit does not limit internal growth by a financial company (i.e., growth other than through acquisitions, consolidations or mergers). The concentration limit is in addition to restrictions that may apply under antitrust or other laws, including the nationwide deposit cap in section 3(d) of the BHC Act.

2. SCOPE OF FINANCIAL COMPANIES SUBJECT TO THE CONCENTRATION LIMIT

Section 622's concentration limit applies only to a "financial company," which is defined in the statute as: (i) any insured depository institution; (ii) any bank holding company; (iii) any savings and loan holding company; (iv) any company that controls an insured depository institution; (v) any nonbank financial company supervised by the Board under title I of the Dodd-Frank Act;[6] and (vi) any foreign bank or company that is treated as a bank holding company for purposes of the BHC Act.[7] Notably, this definition of "financial company" encompasses any type of insured depository institution, including savings associations, limited-purpose trust companies the deposits of which are insured by the Federal Deposit Insurance Corporation ("FDIC"), limited-purpose credit card banks and industrial loan companies that are excluded from the BHC Act's definition of "bank."[8] The definition also includes any company that controls such an insured depository institution, regardless of whether or not that company is, or is treated as, a bank holding company or a savings and loan holding company. Accordingly, commercial or industrial firms (such as retailers and automobile companies) that control an insured depository institution

[5] Id. at § 1852(b).

[6] Section 113 of the Dodd-Frank Act provides the Council with the authority to require that a "nonbank financial company" be subject to supervision and heightened prudential standards issued by the Board if the Council determines that the nonbank financial company could potentially pose a threat to the financial stability of the United States in the event of material financial distress at the nonbank financial company. See Dodd-Frank Act, § 113 (2010).

[7] Under section 8 of the International Banking Act of 1978, a foreign bank or foreign company is subject to the BHC Act in the same manner and to the same extent that bank holding companies are subject to the BHC Act if it, or one of its subsidiaries, is a foreign bank that maintains a branch or agency in the United States or has a commercial lending subsidiary in the United States. See 12 U.S.C. § 3106.

[8] See 12 U.S.C. § 1841(c). We also note that the definition of "financial company" does not encompass credit unions, and companies that control credit unions are not otherwise included in the definition.

(e.g., an industrial loan company or limited-purpose credit card bank) are defined as "financial companies" for purposes of section 622 and subject to the concentration limit, and their liabilities are included in the denominator of the concentration limit for purposes of determining whether other financial companies are in compliance with the limit.

On the other hand, a financial company that is not affiliated with an insured depository institution or a foreign bank with a U.S. banking office is not considered a financial company under section 622, unless the company is designated by the Council as a nonbank financial company subject to the supervision of the Board. As a result, companies that engage in activities that are perceived as "financial" generally speaking, such as insurance or securities firms, but that are not affiliated with an insured depository institution or a foreign bank with a U.S. banking office, are generally not captured by the statutory definition of "financial company." These companies are not subject to the concentration limit and their liabilities are not included in the denominator of the concentration limit for purposes of determining whether other financial companies are in compliance with the limit.

3. CALCULATION OF A FINANCIAL COMPANY'S LIABILITIES

The statutory concentration limit uses a financial company's "liabilities" to measure and limit concentration within the financial sector. Under section 622, as enacted, a financial company's "liabilities" are used to measure both that company's individual size (which we sometimes refer to in this study as the concentration limit "numerator") and the aggregate size of all financial companies (which we sometimes refer to in this study as the concentration limit "denominator"). It should be noted that in most cases the statutory definition of a financial companies liabilities is based on risk-weighted assets and regulatory capital, which are different than liabilities calculated under generally accepted accounting principles ("GAAP"). Section 622, as enacted, defines "liabilities" to mean, with respect to most U.S. financial companies, (i) the total risk-weighted assets of the company, as determined under the risk-based capital rules applicable to bank holding companies (and as adjusted to reflect exposures that are deducted from regulatory capital), less (ii) the total regulatory capital of the company, as determined under the same risk-based capital rules.[9]

The statute defines the liabilities of foreign-based financial companies, insurance companies and nonbank financial companies supervised by the Board slightly differently. For a foreign-based financial company, liabilities are defined by the statute in a manner similar to U.S. financial companies, except that a foreign-based company's risk-weighted assets and regulatory capital: (i) are limited to those "of the United States operations" of the financial company; and (ii) are to be calculated under "applicable" risk-based capital rules.[10] For both insurance companies and nonbank financial companies supervised by the Board, the statute provides that such companies

[9] See 12 U.S.C. § 1852(a)(3)(A). Under the risk-based capital rules applicable to bank holding companies, a firm computes its risk-weighted assets by multiplying each of its balance-sheet assets by a risk weight, reflecting the credit risk of the asset. In addition, a firm must convert each of its off-balance-sheet exposures to an on-balance-sheet equivalent and multiply the resulting amount by the appropriate risk weight. A firm's total risk-weighted assets are the sum of the risk-weighted assets associated with its on-balance-sheet assets and off-balance-sheet exposures.
[10] Id. at § 1852(a)(3)(B).

"liabilities" shall mean "such assets of the company as the Board shall specify by rule, in order to provide for consistent and equitable treatment of such companies."[11]

4. STATUTORY EXCEPTIONS AND INTERPRETATIONS

The statute excepts three types of acquisitions from the concentration limit: (i) an acquisition of a bank in default or in danger of default;[12] (ii) an acquisition with respect to which the FDIC provides assistance under section 13(c) of the Federal Deposit Insurance Act (the "FDI Act"); and (iii) an acquisition that would result only in a de minimis increase in the liabilities of the financial company.[13] A financial company seeking to make an acquisition under any of these three exceptions must obtain the prior written consent of the Board (in addition to any other regulatory notices or approvals otherwise required for the transaction).

[11] Id. at § 1852(a)(3)(C). Unlike the definition of liabilities for purposes of other types of financial companies, which are generally determined by subtracting capital from assets, the definition of liabilities applicable to insurance companies and nonbank financial companies supervised by the Board refers only to assets.

[12] Id. at § 1852(c)(1). We note that this exception applies by its terms to a failing "bank," rather than a failing insured depository institution. Under the BHC Act, within which section 622 is codified, the term "bank" is defined in a manner that excludes certain insured depository institutions, including savings associations, industrial loan companies, credit card banks and limited-purpose trust companies. See 12 U.S.C. § 1841(c).

[13] Id. at § 1852(c). The Board, in establishing a threshold for the de minimis exception, should ensure that the exception does not permit transactions that would be inconsistent with the spirit and purpose of the concentration limit.

PART B: EFFECTS OF THE CONCENTRATION LIMIT

1. OVERALL EFFECTS OF THE CONCENTRATION LIMIT

In the near term, the financial sector concentration limit is likely to prohibit acquisitions by only a small number of financial companies. As described in Part A, the concentration limit applies to insured depository institutions, bank holding companies, savings and loan holding companies, other companies that control an insured depository institution, nonbank financial companies supervised by the Board, and foreign banking organizations that are treated as bank holding companies under the BHC Act. The extent to which the concentration limit may affect the financial sector depends on the extent to which financial companies are (or would become as result of an acquisition) near, at, or over the concentration limit. In the near term, the concentration limit is mostly likely to restrict or otherwise affect acquisitions by four financial institutions–Bank of America Corporation, J.P. Morgan Chase & Company, Citigroup, Inc., and Wells Fargo & Company–because only these four firms, based on current estimates, appear to hold more than 5 percent of the aggregate liabilities of all financial companies subject to the concentration limit.[14] Over time, the concentration limit may affect different or additional firms depending on firms' relative growth.

In 1994, Congress prohibited any bank holding company from making an interstate acquisition of a bank if it would result in the acquirer controlling 10 percent or more of the total insured deposits in the United States. The 10 percent deposit cap was not binding on any firm when it was imposed in 1994, but acquisitions by large commercial banks brought three firms up to the cap, and acquisitions of institutions not covered by the deposit cap put Bank of America above the cap. Growth of deposits generally, as well as each firm's internal growth, could affect these calculations over time. Table 1 gives the year-end deposit shares as measured in the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the "Riegle-Neal Act")[15] deposit-cap calculations from 2003 through 2009 for the four largest depository institutions.[16] Historical deposit shares show a number of large jumps when the four firms have made major acquisitions. Historical trends also indicate that growth of the largest financial institutions has taken place largely through acquisitions and mergers, particularly since the Riegle-Neal Act lifted the statutory restriction on interstate banking combinations. Growth through acquisitions and

[14] As described below in Part C.1, section 622, as enacted, defines "liabilities" by reference to risk-weighted asset and capital figures under risk-based capital rules for many financial companies, but some of those financial companies currently are not required to calculate their risk-weighted assets and capital under risk-based capital rules. As a result, it is not possible to produce precise estimates of the relative concentration among financial companies under section 622, as enacted. For this reason, the Council has recommended in Part C.2.1 that the concentration limit's definition of liabilities applicable to certain financial companies be modified. The Council's initial, preliminary and non-binding estimate of the total liabilities of financial companies under the concentration limit, as of December 31, 2009, but otherwise reflecting the modification recommended by the Council in Part C.2.1, is roughly $14.3 trillion. This figure uses the following measures by category of firm (some of which are estimates): for standalone insured depository institutions and bank holding companies, risk-weighted assets minus capital figures under risk-based capital rules; for savings and loan holding companies and companies that control an insured depository institution that are not or are not treated as a savings and loan holding companies or banking holding companies, GAAP liabilities; for foreign-based firms, total U.S. third party liabilities as reported on U.S. regulatory reporting forms. Data for some privately held parents of industrial loan companies, credit card banks and special purpose trusts are not available from existing regulatory reports or public data sources.

[15] Pub. L. No. 103-328, 108 Stat. 2338 (1994). Currently, the Riegle-Neal Act deposit cap prohibits a depository institution, bank holding company or savings and loan holding company from acquiring or merging with an insured depository institution in another state if, after consummation of the acquisition, the applicant would control more than 10 percent of the total amount of deposits of insured depository institutions in the United States. See 12 U.S.C. §§ 1828(c), 1843(i), and 1467a(e)(2).

[16] National deposit shares as defined by the Riegle-Neal Act were not calculated prior to 2003, because it was obvious from national shares of total deposits that no firm was close to the 10 percent deposit cap.

mergers provides the ability to execute strategic options more quickly than organic growth. As such, it can be expected that large financial organizations would continue to want to make strategic acquisitions in the future.

Although the acquisition of insured deposits is already constrained by the 10 percent nationwide deposit cap imposed by the Riegle-Neal Act, the concentration limit should provide a more comprehensive limitation on growth by acquisition because it also allows non-deposit liabilities and off-balance sheet exposures to be taken into account. Currently, the deposit cap provides incentives for banking firms near, at, or over the cap to shift liabilities from deposits to potentially more volatile on- and off-balance-sheet liabilities. A firm wishing to acquire a banking organization but constrained by the deposit cap can shed deposits in exchange for more volatile liabilities, thereby reducing its national deposit share while maintaining the same volume of total assets. Similarly, because the deposit cap is measured based solely on deposits, it does not constrain a banking organization from increasing its exposure to potentially risky assets, including risky off-balance sheet positions.

The impact of the concentration limit on financial companies at or near the threshold is likely to be muted by the fact that these firms will likely already be constrained by the 10 percent nationwide deposit cap imposed by the Riegle-Neal Act. As a consequence, the incremental effect of the concentration limit in the near term will likely be limited to restricting the largest U.S. banking firms from large acquisitions of foreign firms or non-depository domestic organizations. Because there is no de minimis exemption in the Riegle-Neal Act deposit cap, depository institutions that control more than 10 percent of national deposits can generally acquire only non-insured depository institutions under the Riegle-Neal Act deposit cap.[17]

It is important to note that neither the Riegle-Neal Act deposit cap nor the Dodd-Frank Act concentration limit prevent firms from growing larger through internal, organic growth. Large commercial banks generally have not demonstrated the ability to increase their deposit share substantially through organic growth; instead, they have relied largely on acquisition rather than organic growth to expand. If this pattern continues in the future, the deposit cap and concentration limit could be expected to keep the shares of a financial company that is predominantly engaged in banking from growing significantly above the 10 percent cap in the future.

2. EFFECTS OF THE CONCENTRATION LIMIT ON FUTURE FINANCIAL STABILITY

The concentration limit is likely to promote greater future U.S. financial stability by restricting the rapid growth of the largest firms in the U.S. financial markets. The concentration limit will restrict the ability of the largest financial companies to engage in acquisition transactions that substantially increase their size. Restrictions on future growth by acquisition of the largest financial companies ultimately will prevent acquisitions that could make these firms harder for their officers and directors to manage, for the financial markets to understand and discipline, and for regulators to supervise. The concentration limit, as structured, could also have the beneficial

[17] The Riegle-Neal Act deposit cap applies only to interstate acquisitions of banks, so a firm constrained by the cap is not prohibited from acquiring a bank with positive deposits if that bank is headquartered in the same state as the acquiring firm. Prior to the passage of the Dodd-Frank Act, the deposit cap did not apply to acquisitions of thrift institutions, but section 623 of the Dodd-Frank Act expands application of the deposit cap to acquisitions of any insured depository institution.

effect of causing the largest financial companies to either shed risk or raise capital to create room under the cap. Such actions, other things equal, would tend to reduce the chance that the firm would fail. In addition, as noted earlier, the concentration limit ameliorates the incentive for large financial companies to shift from deposits to potentially less stable liabilities in order to be able to make additional acquisitions.

Because firms with less than 10 percent of U.S. financial liabilities can be sufficiently large or otherwise critical to the functioning of financial markets to raise systemic issues in the event of failure, the concentration limit alone is unlikely to sufficiently reduce the risks posed to financial stability by systemically important firms. But together with other reforms – including the enhanced prudential standards that will apply to bank holding companies with more than $50 billion in assets and nonbank financial companies designated as systemically important firms and the new resolution regime established by title II of the Dodd Frank Act–the concentration limit should help increase future financial stability.

3. EFFECTS OF THE CONCENTRATION LIMIT ON MORAL HAZARD

The overall effect of the concentration limit on moral hazard is expected to be small. While the financial sector concentration limit is expected to moderately decrease the moral hazard associated with the "too-big-to-fail" problem, it also may slightly increase moral hazard in the sector by reducing the likelihood of hostile takeovers of large financial companies.

Moral hazard may be defined as the risk that one party to a transaction behaves differently than it would behave if it fully took into account the risk of the transaction. Moral hazard in the banking industry is often associated with the "too big to fail" problem, where managers, owners, and creditors of large banking organizations benefit from the upside of risk taking, but may expect to bear little cost of the downside in the event of failure, because of the perceived likelihood of government support. As one piece of a coordinated set of legislative and regulatory efforts to end the "too-big-to-fail" problem, the financial sector concentration limit should help reduce the prospects for any increase in implicit subsidy for the nation's largest financial firms going forward and the moral hazard created by the perception that any firm is too big to fail.

Moral hazard also often arises in principal-agent situations, where one party (such as the management of a firm) acts on behalf of another party (such as the owners of a firm). Healthy markets for corporate control can help mitigate the moral hazard problem associated with the separation of ownership and control in publicly traded companies.[18] The concentration limit may cause a modest increase in moral hazard for financial companies that are near, at, or above the limit by eliminating the market discipline that might otherwise be imposed by the potential acquisition of such firms by other financial companies.[19] It is noteworthy, however, that hostile takeovers are quite rare in the U.S. commercial banking industry. This fact further reduces the modest extent to which the concentration limit may increase moral hazard. In addition, all bank holding companies with $50 billion or more in assets are now subject to heightened prudential regulation, which may offset, to some extent, any increase in moral hazard.

[18] Managers who fail to act in the best interest of their shareholders face the threat of hostile takeover and subsequent ouster.
[19] The limit will ultimately make it difficult for any of the largest U.S. banking firms to be acquired by another financial institution, other than a foreign firm with limited U.S. operations, thereby potentially reducing market discipline on the management of these firms.

The concentration limit is likely to have little or no effect on the actions of financial companies that are not constrained by the concentration limit, and will likely neither increase nor decrease the effects of moral hazard on the behavior of such companies. The concentration limit may ultimately reduce the number of potential acquirers for some smaller non-depository financial organizations by the small number of firms that approach or exceed the limit, but a large number of potential acquirers would remain for such firms.

4. EFFECTS OF THE CONCENTRATION LIMIT ON THE EFFICIENCY AND COMPETITIVENESS OF U.S. FINANCIAL FIRMS AND MARKETS

The concentration limit is not expected to significantly affect the efficiency and competitiveness of U.S. markets in the near term because it will constrain the behavior of only a handful of firms that already operate at a very large scale and because the limit does not restrict organic growth by any firm.[20] In addition, based on existing research, there is limited evidence that economies of scale and scope exist in the financial sector beyond modest size levels.[21] Over the long run, however, the concentration limit can be expected to enhance the competitiveness of U.S. financial markets by preventing the increased dominance of those markets by a very small number of firms.

The expected impact of the concentration limit on the competitiveness of U.S. financial firms is more mixed. The concentration limit is expected to improve competition in U.S. financial markets over time by reducing the possibility that one or two firms will dominate the sector. At the same time, the Council is concerned that the limit introduces the potential for disparate regulatory treatment of mergers between the largest U.S. and foreign firms, depending on which firm is the acquirer or the target. Specifically, the statutory concentration limit would allow large foreign-based firms with a small U.S. presence to acquire large U.S. firms, but would prohibit large U.S. firms from acquiring large foreign-based financial firms.

A very extensive empirical literature on economies of scale for commercial banks has found conflicting results. Most research using data from years prior to 2000 found that scale economies disappear long before a firm would become large enough to be bound by the concentration limit.[22] Some research using more recent data has found economies of scale for even the largest banking organizations, though the size of these economies is often modest and may not exist for firms with entrenched management.[23] All such research is limited to data on existing financial institutions, and applying estimates of scale economies from a large sample of smaller firms to the very largest U.S. financial companies runs the risk of applying estimates to firms outside the size range of the sample on which they were computed. Also, as noted earlier, the deposit cap imposed by Riegle-Neal Act could have the same effect on realizing scale economies. A smaller and less current body of research has found little or no evidence of

[20] Efficiency is measured by the amount of output a firm produces for a given amount of inputs. Competitiveness measures the same concept at the market level, measuring how much output all market participants as a group produce from a given amount of inputs.
[21] Two basic concepts in the measurement of efficiency are economies of scale and economies of scope. Scale economies are said to exist if larger firms can produce output at lower average cost of inputs than smaller firms. Scope economies exist if firms that provide a variety of products can produce them at lower average cost than firms that specialize in a narrower range of products.
[22] Most such research finds economies of scale for very small commercial banks and a shallow U-shaped average-cost curve for banks above a minimum-efficient scale. This means that medium-sized banking organizations are slightly more efficient than either small or large firms. Different studies have placed the upper limit on scale economies at from $100 million to $25 billion in assets. While this is a broad range, its upper end is well below the size of banks constrained by the liability cap. A summary of this literature can be found in Group of Ten (2001).
[23] See, e.g., Feng and Serletis (2010), Wheelock and Wilson (2010), and Hughes, Lang, Mester, Moon and Pagano (2003).

economies of scope among financial lines of business.[24] Research on economies of scope is less extensive than that on scale economies and is hampered by the lack of specialized banks to which a bank offering a broader range of products can be compared.[25]

The concentration limit can be expected to enhance the competitiveness of U.S. financial markets over the long run by preventing the increased dominance of those markets by a very small number of firms. Evidence suggests that maintaining a less concentrated market structure in the long run results in more competitive markets.[26] While the small number of firms constrained by the concentration limit may compete less vigorously for some business in order to avoid exceeding the concentration limit, sufficient numbers of competitors not constrained by the cap are likely to exist in financial markets to maintain competitive conditions. Therefore, we would expect competitive benefits from the concentration limit in the long run.

Given the evidence on scale and scope economies, the concentration limit likely will not seriously limit the ability of U.S. financial firms to compete effectively with foreign financial firms. Even the small number of firms subject to the cap can expand internationally through internal growth, such as by establishing new foreign subsidiaries.

The concentration limit, as enacted, treats acquisitions by U.S-based firms and foreign-based firms unequally. The statutory concentration limit includes the global consolidated liabilities of U.S. financial companies but only the liabilities of the U.S. operations of foreign firms. As a result, a large, globally-active U.S. financial company–whose liabilities are measured on a global basis under section 622–could be prevented by the concentration limit from making any material acquisitions (U.S. or foreign), but a large foreign-based financial company with a relatively small U.S. presence may be able to acquire that same U.S. financial company because only the U.S. liabilities of the resulting company would be subject to the concentration limit. In addition, depending on the extent of its U.S. operations, the foreign-based company might be able to continue to acquire U.S. financial companies without running afoul of the concentration limit because, unlike a U.S.-based firm, the foreign operations of the foreign-based company are excluded from the concentration formula. Over time, this disparity could increase the degree to which the largest firms operating in the U.S. financial sector are foreign-based. Further consideration and review of this issue is warranted and the Council recommends that the Board continue to monitor and report on these competitive dynamics. If the Council determines that there are any significant negative effects, the Council will then issue a recommendation to Congress to address adverse competitive dynamics.

[24] See Group of Ten (2001). We note that scope of activities is only relevant to the concentration limit analysis to the extent that it has an indirect, positive relationship to a firm's scale more generally.

[25] There is little empirical research on economies of scale and scope in investment banking, but the research that does exist reaches conclusions that parallel those for commercial banking: there are economies at modest levels of scale and scope, but these are exhausted below the size of the largest firms. Some activities of investment banks, such as foreign exchange trading, appear to offer substantial economies of scale.

[26] A large body of theoretical and empirical work has found that less concentrated markets produce socially beneficial results compared to more concentrated markets. Empirical research using reduced-form analysis has found an economically meaningful relationship between market concentration and prices. In addition, empirical models have been developed in recent years that derive estimates from underlying consumer preferences, firm costs, and interactions among firms. These theoretically derived empirical models allow for a richer characterization of markets; their results are consistent with the idea that more concentrated markets are, in general, associated with higher prices. See Dick and Hannan (2010).

5. EFFECTS OF THE CONCENTRATION LIMIT ON THE COST AND AVAILABILITY OF CREDIT AND OTHER FINANCIAL SERVICES

The concentration limit is unlikely to have a significant effect on the cost and availability of credit and other financial services. In the short run, the concentration limit may marginally reduce the provision of some financial services by the firms that are closest to the limit, if they restrict provision of these services in order to engage in an acquisition without violating the limit. In the long run, it is possible that a small number of other firms may also be constrained by the concentration limit. However, credit markets include large numbers of competitors, so it is not likely that the overall provision of financial services would be adversely affected by the concentration limit.

A few specific credit markets are dominated by the largest U.S. banking firms to a greater extent than are credit markets in general. For example, the four largest U.S. commercial banking firms control 56.6 percent of the market in general purpose credit card purchase volume.[27] Similarly, these four firms originated 58.2 percent of mortgage loans by volume in 2009 and serviced 56.3 percent of such loans.[28] However, even in these markets, firms providing almost one-half of the market are likely to be unaffected by the concentration limit in the short- to medium-run and should be able to fill any competitive void caused by constrained firms that choose to reduce their presence in a particular product line to stay below the concentration limit. The share of the four largest U.S. banking organizations in other markets, such as syndicated lending, is smaller.[29]

If markets for securitized credit card and mortgage loans operate smoothly, the ability of the largest U.S. banks to grow organically and to sell assets in such markets would further limit the effect of the concentration limit on the provision of those types of credit in which the four largest U.S. banking organizations have the largest combined market shares. Thus, even if these firms increase their combined share of the credit card or mortgage market, the ability to sell such loans to other investors allows these firms to continue to supply credit without regard to constraints imposed by the concentration limit.

[27] See Table 2.
[28] See Table 3.
[29] See Table 4.

PART C: RECOMMENDATIONS REGARDING MODIFICATIONS TO THE CONCENTRATION LIMIT

As noted previously, Congress specifically directed the Council to, concurrent with its study, "make recommendations regarding any modification to the concentration limit that the Council determines would more effectively implement [section 622]."[30] In addition, Congress specifically made the operative part of the statutory concentration limit itself "[s]ubject to the recommendations of the Council," and directed the Board to issue regulations implementing section 622 that "reflect" and are "in accordance with the recommendations of the Council."[31] In considering potential modifications to the concentration limit that might more effectively implement section 622 as enacted, the Council has taken note of the specific topics that Congress required the Council to address in this study–the extent to which the concentration limit under this section would affect financial stability, moral hazard in the financial system, the efficiency and competitiveness of United States financial firms and financial markets, and the cost and availability of credit and other financial services to households and businesses in the United States. The Council believes that the Congressional mandate to consider these factors strongly suggests that Congress intended section 622 to (i) promote financial stability, (ii) limit moral hazard, (iii) promote the efficiency and competitiveness of United States financial firms and financial markets, and (iv) improve, or at least not unduly constrain, the cost and availability of credit and other financial services to households and businesses in the United States.

Taking these considerations into account, the Council has focused on potential modifications that it believes would implement section 622 in the most effective way by mitigating practical difficulties likely to arise in the administration and enforcement of the concentration limit, without undermining its effectiveness in limiting excessive concentration among financial companies. In doing so, the Council has identified a number of implementation issues posed by section 622 as enacted; these implementation issues are summarized below in Part C.1. In light of these and other issues considered by the Council, the Council has decided to recommend three modifications that it believes would more effectively implement section 622. The formal terms of each of these recommended modifications are included below in Part C.2, along with a discussion of the Council's reasons for recommending them.

1. IMPLEMENTATION ISSUES

Substantial challenges exist to implementing the concentration limit in the precise form enacted. For example, as described in Part A, the statute generally uses a financial company's "liabilities" to measure and limit financial sector concentration, and defines this term in specific and different ways with respect to different types of financial companies. For a U.S.-based firm (other than an insurance company or nonbank financial company supervised by the Board), the statute defines liabilities by reference to risk-weighted assets and regulatory capital figures determined under the risk-based capital rules applicable to bank holding companies. As discussed above, risk-weighted assets are calculated by applying specific weights to different types of on- and off-

[30] 12 U.S.C. § 1852(e).
[31] 12 U.S.C. § 1852(c), (e).

balance sheet positions that reflect the inherent risk in those positions. The use of risk-weighted assets and regulatory capital allows the concentration limit to capture the relative riskiness of firms, as well as off-balance-sheet exposures that would not be included in a simple accounting measure of liabilities.

However, a number of companies that are included in section 622's definition of "financial company" are not required to, and do not calculate, consolidated risk-based capital figures under the rules applicable to bank holding companies. In particular, U.S. companies that control an insured depository institution but are not, and are not treated as, bank holding companies currently are not required to calculate or report consolidated risk-based capital figures under the risk-based rules applicable to bank holding companies. Such companies include both savings and loan holding companies and firms that own or control industrial loan companies or limited-purpose credit card banks. Because these companies currently are not required to calculate or report consolidated risk-based capital figures, it is not currently possible to apply the statutory definition of liabilities to all financial companies subject to section 622's concentration limit as a practical matter.[32]

With respect to savings and loan holding companies, this practical problem is only transitional, as other provisions of the Dodd-Frank Act will require these companies to calculate risk-weighted assets and regulatory capital in the future. Section 171 of the Dodd-Frank Act requires that savings and loan holding companies become subject to risk-based capital requirements that are no less than the minimum risk-based capital requirements that were generally applicable to insured depository institutions on the date of enactment of the Dodd-Frank Act.[33] Accordingly, savings and loan holding companies will become subject to risk-based capital rules in the future, at which time these companies' risk-weighted assets and regulatory capital figures may be used in calculating and applying the concentration limit.

With respect to companies that own an insured depository institution but are not, and are not treated as, bank holding companies or savings and loan holding companies (e.g., companies that own industrial loan companies or limited-purpose credit card banks), these companies are not currently subject to, and are not legally required to become subject to, risk-based capital rules. As a result, the practical problems posed in applying the statutory definition of liabilities to these companies are not merely transitional. However, many of these firms are predominantly nonfinancial, and total GAAP liabilities are a much closer proxy for the statutory definition of liabilities for these firms than for firms that are predominantly financial, due to the more limited off-balance-sheet activities of nonfinancial firms and the fact that the assets of these firms would likely receive a 100 percent risk weight under the risk-based capital rules applicable to bank holding companies.

[32] In the case of a foreign-based financial company, section 622 limits the definition of liabilities to the risk-weighted assets and regulatory capital of the company's U.S. operations, and does not include the company's foreign assets and regulatory capital. However, the foreign-based companies subject to section 622's concentration limit generally do not, and are not required under U.S. or foreign law to, distinguish between assets and/or capital that are attributable to U.S. versus non-U.S. operations, respectively. The Board, as the appropriate Federal banking agency for those foreign banking organizations that are subject to the concentration limit (because they are, or are treated as, bank holding companies) has the authority to require such foreign banking organizations to compute risk-weighted assets and regulatory capital for their U.S. operations.

[33] See Dodd Frank Act, § 171 (2010). Section 616 of the Dodd-Frank Act also authorizes the appropriate Federal banking agency for savings and loan holding companies to establish consolidated capital requirements for these companies. See Dodd Frank Act, § 616 (2010). The Council also notes that Section 171 requires that nonbank financial companies supervised by the Board become subject to risk-based capital rules that are no less than the minimum risk-based capital requirements that were generally applicable to insured depository institutions on the date of enactment of the Dodd-Frank Act.

Section 622 as enacted requires that the concentration limit be applied by reference to "the aggregate consolidated liabilities of all financial companies at the end of the calendar year preceding the transaction." This provision may make it difficult or impossible for the Board and any financial company to determine whether a transaction to be consummated early in a calendar year would comply with the concentration limit because of delays in the reporting of data that would be necessary for calculating the limit. In the early portion of any given year, information regarding the liabilities of financial companies, whether individually or in the aggregate, will not yet be available. For example, bank holding companies and companies treated as bank holding companies generally are not required to calculate and report final risk-based capital figures for December 31 until February 14 of the following year,[34] and insured depository institutions generally are not required to calculate and report final risk-based capital figures for December 31 until January 30 of the following year.[35] Additional time is required for Federal banking agencies to review and validate this information. In addition, public financial companies that are required to file periodic reports with the Securities and Exchange Commission under the Securities Exchange Act of 1934 are not required to file their financial statements (including GAAP-based asset and capital figures) for December 31 of any given year until 60 to 90 days thereafter.[36] As a result, data needed to calculate or estimate the aggregate consolidated liabilities of all financial companies at the end of any calendar year may not be available for some time after that date. The Council is also concerned that applying the denominator for any given year as of a single date (i.e., the end of the calendar year) may introduce unnecessary volatility into the concentration limit and its application, particularly given the large increase or decrease to the denominator that might occur from year to year as the result of specific events, such as the designation of a large nonbank financial company as systemically important by the Council, the rescission of such a designation, or the acquisition (or sale) of a bank by a large company that causes it to be newly included (or excluded) from the concentration limit denominator.

Lastly, the concentration limit does not restrict an acquisition of a "bank" (as that term is defined in the BHC Act) in default or in danger of default, subject to the prior written consent of the Board. However, this exception applies by its terms to a failing "bank," rather than all types of failing insured depository institutions, including savings associations, industrial loan companies, limited-purpose credit card banks and limited-purpose trust companies. However, the same strong public interest in limiting the costs to the Deposit Insurance Fund that could arise if a bank were to fail likely applies to insured depository institutions generally.

2. RECOMMENDED MODIFICATIONS TO THE CONCENTRATION LIMIT

2.1. DEFINITION OF "LIABILITIES" FOR CERTAIN COMPANIES

***Council Recommendation**: The concentration limit under Section 622 should be modified so that the liabilities of any financial company (other than an insurance company, a nonbank financial company supervised by the Board, or a foreign bank or a foreign-based financial*

[34] See Instructions to Federal Register Form FR Y-9C at GEN-3; Instructions to Federal Register Form FR Y-9SP at GEN-3.
[35] See, e.g., Instructions to FFIEC Form 041, Consolidated Report of Condition and Income, at 7.
[36] See General Instructions to Securities and Exchange Commission Form 10-K, Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, at 1.

company that is or is treated as a bank holding company) that is not subject to consolidated risk-based capital rules that are substantially similar to those applicable to bank holding companies shall be calculated for purposes of the concentration limit pursuant to GAAP or other appropriate accounting standards applicable to such company, until such time that these companies may be subject to risk-based capital rules or are required to report risk-weighted assets and regulatory capital.

Discussion: As described in Part C.1, although the statutory provisions of section 622 generally define a financial company's "liabilities" by reference to risk-weighted asset and regulatory capital figures under applicable risk-based capital rules, several types of financial companies subject to section 622's concentration limit are not currently subject to consolidated risk-based capital rules. The statutory language's incorporation of regulatory capital figures that are not readily available for certain financial companies poses a substantial practical obstacle to both the accurate calculation of an individual financial company's liabilities for purposes of the concentration limit and the collection and calculation of the aggregate consolidated liabilities of all financial companies for purposes of monitoring compliance with the concentration limit generally.

The Council believes that, given the substantial impact that the concentration limit may have on individual financial companies and the structure of the financial sector, it is fundamentally important that the concentration limit be implemented in a manner that is workable and transparent, both in the immediate future and over time. In particular, the Council believes that in order for the concentration limit to be effective, financial companies must be able to reasonably estimate whether and to what extent their activities are constrained by the concentration limit, and the Board must be able to effectively and efficiently monitor and enforce compliance with the concentration limit. As a result, the Council believes modifying the statutory definition of "liabilities" with respect to certain financial companies, so as to ensure that the liabilities of all financial companies subject to the concentration limit can be reasonably determined and calculated, is necessary to effectively implement section 622.

Specifically, the Council recommends that the Board's rules implementing section 622 provide that, with respect to any financial company (other than an insurance company, a nonbank financial company supervised by the Board, or a foreign bank or foreign-based financial company that is or is treated as a bank holding company) that is not subject to consolidated risk-based capital rules that are substantially similar to those applicable to bank holding companies, the "liabilities" of such a company be calculated pursuant to GAAP or, where GAAP is not applicable, other appropriate accounting standards applicable to such company.[37]

In setting forth this recommendation, the Council is aware of the statutory definition of liabilities set forth in section 622 and, as described above, that for certain types of financial companies the required information is currently not calculated or reported. Therefore, the

[37] Foreign-based financial companies that are or are treated as a bank holding company are not included within the scope of this recommendation because section 622 specifies that the liabilities of such companies shall be determined under "applicable" risk-based capital rules. Insurance companies and nonbank financial companies are not included because section 622 specifies that the liabilities of such companies shall be such assets of the company as the Board may specify by rule. See 12 U.S.C. § 1852(a)(3)(B), (C). Accordingly, the statute as enacted should provide the Board with sufficient flexibility to specify the manner in which the liabilities of these companies should be calculated to allow effective implementation of section 622.

Council is recommending a "hybrid approach," which will use the statutory definition of liabilities for those entities that currently calculate and report risk-weighted assets and regulatory capital figures determined under the risk-based capital rules, and GAAP liabilities for all other financial companies. As described below, liabilities calculated under GAAP can be different from liabilities calculated under risk-based capital rules. For example, under the risk-based capital approach required by the statutory definition of liabilities, the liabilities of bank holding companies are, in the aggregate, 37% less than the amount calculated under GAAP. The same adjustment would not be applicable for entities to which the GAAP approach would apply, thought it is unclear whether the difference between liabilities under a risk-based capital approach and under GAAP would be significant for financial companies that would follow the GAAP approach under the proposed modification because many of those companies are commercial or retail entities that hold assets that are largely or exclusively subject to the high risk-weighting under risk-based capital rules.[38]

In practice, this will produce a test that uses the following measures:

- For stand-alone U.S. insured depository institutions, the existing statutory definition of liabilities for these companies (i.e., risk-weighted assets less regulatory capital);[39]
- For U.S. bank holding companies, the existing statutory definition of liabilities for these companies; [40]
- For U.S. nonbank financial companies designated by the Council, the existing statutory definition of liabilities for these companies;[41]
- For U.S. savings and loan holding companies, the existing statutory definition of liabilities for these companies (other than during the transitional period before these companies become subject to risk-based capital rules as required under other provisions of the Dodd-Frank Act, during which time GAAP (or other applicable accounting standards) liabilities will be used);
- For U.S. and foreign financial companies that own an insured depository institution but are not, and are not treated as, a bank holding company or savings and loan holding company, GAAP liabilities; and
- For foreign-based companies that are, or are treated as, bank holding companies, the existing statutory definition of liabilities for these companies.[42]

The Council believes that the impact noted above will be temporary, as savings and loan holding companies, which as of December 31, 2009 total an estimated 394 financial companies (5.5 percent of the financial companies in the study), but make up an estimated 24.3 percent of the total financial company liabilities under the hybrid approach, would be required as a result of section 171 of the Dodd-Frank Act, to calculate and report statutory liabilities pursuant to a risk-based capital approach. In addition, the Council believes that to address implementation issues with respect to foreign banking organizations, the Board

[38] See Table 5 for an overview of the difference between liabilities calculated under GAAP and risk-based capital rules.
[39] See 12 U.S.C. § 1852(a)(3)(A)).
[40] See id.
[41] See 12 U.S.C. § 1852(a)(3)(C)).
[42] See 12 U.S.C. § 1852(a)(3)(C)). It will be necessary to estimate the risk-weighted assets and regulatory capital of the U.S. operations of such foreign-based companies until such time that this information is available.

should use its authority to collect information from foreign banking organizations about the amount of risk-weighted assets and regulatory capital attributable to the organizations' U.S. operations.

Therefore, after this transitional period, over 99 percent of the number of financial companies will be calculating and reporting statutory liabilities. Accordingly, the concentration limit will be more consistent, with only an estimated 42 entities reporting GAAP liabilities, making up 3.8 percent of the estimated aggregate financial companies liabilities (as of December 21, 2009) under the hybrid method.

In implementing this recommended modification, the Council believes that the Board should, through implementing regulations or guidance, address (i) what other accounting standards may be appropriate for calculating liabilities in this manner and (ii) what GAAP or other accounting financial measures should be used in determining liabilities (e.g., assets and shareholders' equity).

The Council believes that the recommended approach has a number of benefits. First, it leaves the statutory definition of "liabilities" intact for all financial companies that already calculate regulatory capital figures in substantially the same manner as bank holding companies. Second, for firms within the scope of the recommendation that do not calculate regulatory capital figures, the use of appropriate, applicable accounting principles (i) makes use of figures that financial companies already calculate and, in many cases, disclose to the public or shareholders, and (ii) does not require a series of assumptions that could undermine the integrity and transparency of the calculation. The Council believes that this recommended modification would more effectively implement section 622's concentration limit by making it possible for financial companies to monitor and comply with the concentration limit and for the Board to test and enforce such companies' compliance, without undermining either section 622's fundamental purpose and function in limiting concentration among financial companies or the fairness of the concentration limit as applied to different financial companies.

In considering whether to adopt the recommendation, the Council considered the potential impact of the recommended approach on the extent to which the concentration limit may bind large financial companies, particularly during the transitional period. As described above, total GAAP liabilities will not perfectly mirror financial liabilities measured by risk-weighted assets minus regulatory capital for firms that are not currently subject to risk-based capital rules. GAAP assets may be higher for a particular firm than assets calculated under risk-based capital rules because low-risk assets or exposures of the company may be assigned low risk-weights under risk-based capital rules. Conversely, GAAP assets may be lower for a particular firm than assets calculated under risk-based capital rules because off-balance sheet positions of the company are reflected under risk-based capital rules. As a result, to the extent that the liabilities of financial companies subject to this recommendation were, in the aggregate, larger under GAAP than they would be if calculated under risk-based capital rules, this would make the concentration limit denominator larger. This could have the effect of permitting a large financial company, particularly during the transition period, to make an acquisition that might otherwise be prohibited if risk-weighted assets and regulatory capital figures were immediately available for all firms.

Nevertheless, the Council believes that the transparency, consistency and reliability associated with this approach are preferable to employing a series of assumptions about what the risk-based capital profile of firms that do not calculate risk-based capital figures would likely be. Moreover, the Council emphasizes that this recommendation is principally transitional in effect, as it only applies for so long as the specified financial companies are not subject to risk-based capital rules that are substantially the same as those applicable to bank holding companies. For example, as stated above, once savings and loan holding companies become subject to risk-based capital rules, the liabilities of such companies would, in accordance with the Council's recommendation, be calculated under those risk-based capital rules in accordance with the statutory definition of liabilities. As a result, the Council expects the population of financial companies included in the concentration limit that will not be subject to risk-based capital rules (and thus, for which GAAP liabilities will be used) is very small, constituting only an estimated 3.8 percent of the total concentration limit denominator as calculated under the recommendation modification as of December 31, 2009.

In order to ensure that appropriate financial information under applicable accounting principles is available for companies not currently subject to risk-based capital rules, the Council encourages the Board, the FDIC and the Office of the Comptroller of the Currency to collect this information by requiring each insured depository institution that is not controlled by a bank holding company, a company treated as a bank holding company, or a savings and loan holding company to report the total consolidated liabilities of its top-tier parent company as of the end of each calendar year based on the appropriate accounting standards and, to the extent possible, to use publicly reported data.

2.2. Collection, Aggregation and Public Dissemination of Concentration Limit Data

Council Recommendation: *The concentration limit under Section 622 should be modified to provide that a transaction covered by section 622 shall be considered to have violated the concentration limit if the total consolidated liabilities of the acquiring financial company upon consummation of the transaction would exceed 10 percent of the average amount of aggregate consolidated liabilities of all financial companies as reported by the Board as of the end of the two most recent calendar years. For this purpose, rules issued under section 622 shall provide for the Board to publicly report, on an annual basis and no later than July 1 of any calendar year, a final calculation of the aggregate consolidated liabilities of all financial companies as of the end of the preceding calendar year.*

Discussion: As described in Part C.1, although the statutory provisions of section 622 require a financial company to comply with the concentration limit with respect to aggregate financial company liabilities as of the end of the most recent calendar year, the data necessary to determine such aggregate liabilities will not be publicly available for some time following the end of the calendar year. In addition, it is likely that the Board will require an additional period of time, perhaps 2 to 3 months, to aggregate all available data and verify and publish an aggregate financial company liabilities figure. Until such data are compiled,

certified, and made available, financial companies will, at best, only be able to estimate whether a transaction would comply with the limit.

In addition, the Council is concerned that applying the denominator for any given year as of a single date (i.e., the end of the calendar year) may introduce unnecessary volatility into the concentration limit and its application, particularly given the large increase or decrease to the denominator that might occur from year to year as the result of specific events, such as the designation of a large nonbank financial company as systemically important by the Council, the rescission of such a designation, or the acquisition (or sale) of a bank by a large company that causes it to be newly included (or excluded) from the concentration limit denominator. To address this concern, the Council recommends that the Board, in implementing section 622, use the average of the final aggregate financial company liabilities figure as of the end of the prior 2 years as the denominator in the concentration limit, rather than just using the aggregate financial company liabilities figure as of the end of the prior year.

As a result, the Council recommends that the statutory provision be modified to provide that a transaction covered by section 622 shall be considered to have violated the concentration limit if the total consolidated liabilities of the acquiring financial company upon consummation of the transaction would exceed 10 percent of the average amount of aggregate consolidated liabilities of all financial companies as reported by the Board as of the end of the two most recent calendar years. This will reduce the volatility of the denominator of the concentration limit and will ensure that the applicable denominator is at all times transparent and known to each financial company subject to the concentration limit.

In addition, the Council believes that the Board should make a final denominator amount public on an annual basis, which upon publication would be the legally effective denominator (subject to the averaging discussed in the preceding paragraph) beginning on that date and continuing until the next annual final denominator amount is made public by the Board. Separate from and in addition to publication of this legally effective denominator figure, in order to provide financial companies with as much advance notice as possible as to what the denominator amount is likely to be, the Council encourages the Board to consider making public an initial, nonbinding and estimated denominator amount in advance of the final figure. The Council believes that its recommended approach will both resolve the practical problems posed by the statutory provisions on this point and help ensure that the concentration limit is implemented and enforced in a fair and transparent fashion around which financial companies can organize meaningful compliance efforts.

2.3. ACQUISITION OF FAILING INSURED DEPOSITORY INSTITUTIONS

Council Recommendation: *The concentration limit under section 622 should be modified to provide that, with the prior written consent of the Board, the concentration limit shall not apply to an acquisition of any type of insured depository institution in default or in danger of default.*

Discussion: As described in Part A, the statute includes an exception from the concentration limit for an acquisition of a bank in default or in danger of default, subject to the prior written

consent of the Board.[43] However, this exception applies by its terms to a failing "bank," rather than a failing insured depository institution. Under the BHC Act (within which section 622 is codified) the term "bank" is defined in a manner that excludes certain insured depository institutions, including savings associations, industrial loan companies, limited-purpose credit card banks and limited-purpose trust companies.[44] The Council believes that the important policy that supports the exception for the acquisition of failing banks–namely, the strong public interest in limiting the costs to the Deposit Insurance Fund that could arise if a bank were to fail, which might be partly or wholly limited through acquisition of a failing bank by another firm–applies equally to insured depository institutions generally, and is not limited to "banks" as that terms in defined in the BHC Act. Accordingly, the Council recommends that the concentration limit be modified to except from the concentration limit an acquisition of a failing insured depository institution. As with the other statutory exceptions, use of this exception would require the prior written consent of the Board in any specific instance. Such approval would be in addition to any other regulatory approvals required for the transaction.

[43] Id. at § 1852(c)(1).
[44] See 12 U.S.C. § 1841(c).

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FIGURES

FIGURE 1: NATIONAL DEPOSIT SHARES OF THE FOUR LARGEST DEPOSITORY INSTITUTIONS

	2003	2004	2005	2006	2007	2008	2009
Bank of America	7.41	9.99	8.99	9.06	10.01	10.61	11.99
Wells Fargo	4.55	4.61	4.78	4.27	4.15	9.90	9.94
J.P. Morgan Chase	3.76	6.83	6.92	7.23	7.43	9.99	8.49
Citigroup	3.55	3.45	3.50	3.766	4.24	4.36	4.26

SOURCE: Reports of Income and Condition and equivalent reports from thrift institution

FIGURE 2: U.S. GENERAL PURPOSE CREDIT CARD PURCHASE VOLUME

	2009 Market Shares (%)
American Express	23.27
J.P. Morgan Chase	17.85
Bank of America	12.88
Citigroup	10.70
Capital One	5.31
Discover	4.97
U.S. Bank	3.85
Wells Fargo	2.63
HSBC	1.91
Barclays	1.64
USAA	1.44
GE Money	1.03

SOURCE: Nilson Report

FIGURE 3: MORTGAGE ORIGINATIONS AND SERVICING, 2009

	Market Share (%)	
	Originations	Servicing
Wells Fargo	23.5	16.7
Bank of America	21.6	20.0
J.P. Morgan Chase	8.6	12.9
Citigroup	4.5	6.7
GMAC	3.5	3.2
US Bank	3.1	1.6
SunTrust Mortgage Inc	2.8	1.6
Provident Funding	2.1	0.4
USAA Federal Savings Bank	2.1	0.2
PHH Mortgage	2.0	1.4

SOURCE: Mortgage Market Statistical Annual

FIGURE 4: SYNDICATED LENDING MARKET SHARES

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
J.P. Morgan Chase	3.9	25.0	27.1	24.0	19.0	19.6	15.5	14.7	12.0	8.9	8.9
Citigroup	9.1	12.0	15.9	13.4	13.8	12.7	12.3	10.6	9.9	7.5	6.9
Bank of America	11.2	12.9	13.3	10.9	9.6	11.0	9.4	8.9	7.2	5.6	6.9
BNP Paribas Group	2.3	1.6	1.8	2.6	3.0	3.3	3.5	3.6	3.6	4.6	5.3
RBS	1.5	1.4	1.4	2.3	2.2	2.7	3.5	4.7	4.1	6.2	4.0
Barclays Capital	1.6	3.0	2.7	4.3	4.6	4.1	3.7	3.2	2.9	3.4	3.1
Credit Agricole CIB	0.0	0.0	0.0	0.0	2.1	2.0	2.6	1.9	2.1	2.7	3.1
HSBC Bank PLC	1.5	2.0	1.6	2.5	3.4	2.4	2.5	2.2	1.8	2.6	3.0
Deutsche Bank AG	4.9	4.0	4.6	5.4	4.0	3.7	3.6	4.0	3.8	3.1	2.8
Wells Fargo & Co	0.1	0.3	0.4	0.5	0.6	0.8	0.7	0.7	0.5	0.7	2.4

NOTE: Market shares are measured by syndicated lending volume as reported by Bloomberg. Bank of America's share for 2009 includes Merrill Lynch.

FIGURE 5: ESTIMATED DIFFERENCE BETWEEN GAAP AND RISK-BASED CAPITAL LIABILITY MEASURES BY CATEGORY OF COMPANIES

Preliminary and Non-Binding Estimates

Categories of Companies (US$ billions)	Number of Companies	Total Liabilities under GAAP ("GAAP Liabilities")	Risk-Weighted Assets less Regulatory Capital ("RWA-RC Liabilities")	Percentage Difference between GAAP Liabilities and RWA-RC Liabilities	Liabilities under the Recommended Modification to the Definition of Liabilities in Part C.2.1
Stand-alone Insured Depository Institutions ("IDIs")	1,711	368	237	-35.5%	237
Bank Holding Companies ("BHCs")	4,886	13,267	8,293	-37.5%	8,293
Savings and Loan Holding Companies ("SHLCs")	394	3,465	N/A	N/A	3,465
Companies that control IDIs but are not, and are not treated as, BHCs or SLHCs	42	551	N/A	N/A	551
Foreign Banking Organizations*	178	N/A	N/A	N/A	N/A

NOTE: Liabilities under the recommended modification to the definition of liabilities in Part C.2.1 are:

- *Risk-weighted assets minus risk-based capital for BHCs and stand alone insured depository institutions, and*
- *GAAP liabilities for SLHCs and companies that control an IDI but are not and are not treated as BHCs or SLHCs.*

* For foreign-based firms, liabilities will be estimated using U.S. third party liabilities or other appropriate methods as reported on U.S. bank regulatory forms until risk-weighted assets and capital figures under risk-based capital rules are reported on a U.S. operations basis. The complete information that is required to calculate U.S.-only liabilities under GAAP or risk-based capital rules is not currently available.