

Testimony of

James E. Smith

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Financial Institutions Subcommittee

of the

Banking, Housing and Urban Affairs Committee

United States Senate

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Mr. Chairman, I am James E. Smith, Chairman and CEO of Citizens Union State Bank and Trust, Clinton, Missouri and the President of the American Bankers Association. I am pleased to be here today on behalf of the American Bankers Association (ABA). ABA brings together all elements of the banking community to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional, and money center banks and holding companies, as well as savings institutions, trust companies, and savings banks – makes ABA the largest banking trade association in the country.

I want to thank you, Mr. Chairman, for holding this hearing. It allows all parties to get beyond the heated rhetoric and focus on the issues. In the debate over allowing banks to engage in real estate brokerage, we bankers have sometimes been portrayed as somehow working against real estate agents. We disagree with this characterization. The reality is that many agents and bankers already work closely with one another. In fact, I believe that bankers and many in the real estate industry are much closer aligned on the issue of real estate brokerage than the rhetoric suggests. We all believe that customers deserve to have the best possible service, regardless of what company provides it. We all want customers to have many choices of whom to deal with so they can seek out that agent or company that they trust. And we all believe that the provision of any financial service should be done in a safe and sound manner – including adhering to all licensing, qualification, sales practices, and continuing education requirements.

If banking institutions offer real estate brokerage and management services there would be more choices available for everyone. Consumers would have more choices of real estate firms when buying or selling a home. Real estate brokers would have more choices of potential employers. And real estate companies would have more choices of companies to partner with that could provide new sources of capital and technology. By prohibiting bank involvement, S. 1839 would do just the opposite – consumers, real estate agents and real estate companies would have **fewer** choices. We believe a competitive market is the best way to provide quality real estate brokerage and management services.

As we begin our discussion, it is important to note that combining real estate brokerage and banking services is not a new or unusual activity. Real estate firms do it. Insurance companies do it. Securities firms do it. And well over half the federally insured depository institutions in this country, including many of the largest banks and savings institutions, have authority to do it. In fact, my community bank in Missouri has the authority to do it. The ABA believes that **all** banking institutions should have the same opportunity to provide services that meet the needs of our customers.

This issue of open and fair competition is not new – in fact, it has been debated in this legislative body for many years. However, the statutory context within which today’s discussion will take place is quite different. In 1999, Congress took an historic step to modernize the regulation of the financial services sector by passing the Gramm-Leach-Bliley Act (GLB Act). In the more than 15 years of debate on the Act, Congress often found itself in the middle of arguments between financial services industries about who should do what. The result was gridlock and an out-of-date financial system that did not reflect changes in consumer needs or in the use of technology.

To be sure that the pro-competitive goals of the GLB Act continued to be met in a dynamic marketplace, Congress established a flexible, yet conservative regulatory process that would permit the financial industry to offer new services without the need for further legislation. This regulatory system gives the Federal Reserve and Treasury the **flexibility and responsibility** to determine what activities should be approved, including considering what is necessary to permit financial holding companies and national bank subsidiaries to “compete effectively with any company seeking to

provide financial services in the U.S.” This authority is consistent with the Federal Reserve’s and Treasury’s role to ensure efficient, safe, and competitive financial markets.

The GLB Act promotes competition and safety and soundness and enables Congress to avoid becoming embroiled in every competitive issue. ***S. 1839 would take out the flexibility built into this new system, and put Congress back in as referee for future competitive disputes.*** Simply put, the bill would reverse the most important long-term provision in the GLB Act over the very first proposal put forth under it. Having worked so hard to develop a mechanism to keep our financial system up-to-date on an ongoing basis, Congress should not reverse itself less than three years later because some group wishes to protect itself from competition. The system established in the GLB Act should be allowed to work and S. 1839 should not be enacted.

Banking institutions should be allowed to offer real estate services for three key reasons:

- ***It’s good for consumers*** – It means more choices, better service, competitive prices and greater convenience.
- ***It’s only fair*** – Since real estate firms offer banking and insurance services, it’s only fair that banking institutions be allowed to provide real estate services. This is what the Gramm-Leach-Bliley Act is all about – promoting free and fair competition by leveling the playing field.
- ***It’s safe*** – All consumer protections, ***including all state licensing, qualification, sales practices, and continuing education requirements, plus strict privacy laws and anti-tying rules***, would apply to bank-affiliated real estate agents. And because brokerage and management are agency activities, they pose no risk to the bank.

I will discuss these points in detail in the remainder of my statement. Before I do, let me assure you that the competitive issues we are talking about here this morning are important to banks

of all sizes. In fact, the ability to offer real estate brokerage may be more important for smaller institutions. Rural communities may lack real estate agents or are served only by branches of brokers in other towns because there is insufficient business to warrant a local brokerage office. In such small communities, the bank is perceived as the place that will have the greatest amount of information on what properties are for sale, including farmland acreage in agricultural communities. I believe, as do my fellow colleagues who run small community financial institutions, that these services would significantly benefit our customers and our communities.

I. Competition is Good for Consumers

The benefits of competition are well known. In a free market, businesses choose to offer new products if they believe they can provide better services at competitive prices. Obviously, not all banking organizations will choose to offer real estate services, but those that do will enter the market because they believe they can meet or beat the competition. Increasing the number of providers raises the bar for all the participants, forcing improvements in efficiency, pricing and service levels – ***all to the benefit of homebuyers and sellers.***

Allowing all banking institutions to provide real estate services expands the choices for everyone: consumers, real estate agents and real estate companies. This is not only the opinion of bankers, but increasingly, it is a view shared by real estate agents and particularly real estate companies.

More Choices for Consumers, Real Estate Agents and Realty Companies

If banking institutions were allowed to offer real estate brokerage and management services there would be more choices for everyone.

➤ *More Choices for Consumers*

More players in the real estate business mean more and better products for consumers. In any competitive market, new participants bring new, creative ideas to the market – all designed to provide better service and greater convenience, at reasonable prices. In fact,

businesses can only be successful in new markets by providing services that meet the needs of customers. Free competition among a wide variety of providers is the cornerstone of our economic system.

➤ ***More Choices for Real Estate Agents***

Real estate agents pride themselves on being independent contractors, choosing the best companies to work for. If there are more companies to choose from, agents' employment opportunities will be much broader. Banks will only be able to attract good agents by offering competitive commissions and other incentive-based compensation packages. And because the real estate business requires expertise, licensing, and other requirements, banks would seek out experienced real estate agents. Banks know that converting tellers to real estate agents would be a poor business strategy.

➤ ***More Choices for Real Estate Companies***

Forward-looking businesses are always looking for opportunities to improve their franchise value – strengthening, expanding, merging, or even selling their business. Allowing banking institutions to engage in real estate brokerage and management services gives real estate companies more options for bringing additional capital and technology to the table, through joint ventures, for example. Banking institutions also represent potential buyers if agencies choose to sell their businesses. ***Indeed, in some communities, partnering with the local bank may be the only way for the local real estate broker to compete with the growing national chains.*** This is why many real estate firms also oppose S. 1839. It is interesting to note that many insurance agencies thought that bank involvement was going to hurt their business – until they realized that it provided many more options than they had before. To that end, the Financial Service Coordinating Council, consisting of the ABA, the American Council of Life Insurers, the American Insurance Association, and the Securities Industry Association, supports open competition and is on record opposing S. 1839.¹

S. 1839 reduces choices: consumers would have fewer choices of whom to do business with, agents would have fewer choices of whom to work for, and businesses would have fewer

¹ The letter, dated January 16, 2002, is attached to this testimony

choices for joint marketing, fewer potential merger partners, and fewer potential buyers. ABA believes a competitive market is the best way to provide quality real estate brokerage and management services – simply put, more competition means more choices.

Many Real Estate Agents Support Open Competition

Many agents and real estate companies are not concerned by the prospect of banking organizations offering real estate services. Many look forward to the opportunity to partner with a local bank. Independent agents who provide good service today know that they will be competitive with **anyone**, whether the competitor is another independent agent or one affiliated with a bank. The views of these real estate agents are often lost in the emotional rhetoric of their trade association. Here are a few examples of comments filed by real estate agents with the regulators on this proposal:

- A broker from California writes: “Additional competition will be healthy for the industry. Banks and other financial institutions have learned how to meet the needs of consumers and to handle their financial matters. One’s home is the biggest financial asset most consumers will ever deal with. If agents are so special for consumers, then they have nothing to fear. Maybe we could see commissions come down!”
- A real estate broker in North Carolina writes: “I am a 38-year veteran of the real estate industry and do not agree with our National Association of [Realtors]...There are several reasons I feel this way, primarily because our small family-owned business has always faced stiff competition from large real estate firms, yet we have been able to earn a good, honest living. I believe that competition is the American way and if you’re good at what you do, you can survive whether large or small.”
- Another real estate agent notes: “I would welcome the hopefully more professional business management that banks would likely bring to this business. With most real estate being part-time people with limited training, the real estate business is full of mis-information, poor service, etc., a situation that could be improved with bank

- involvement. Furthermore, the American consumer deserves more true competition in this business. Bank owned real estate agencies may be able to lower transactions costs to consumers through aggregation of services benefiting the public as a whole.”
- A real estate broker in Wisconsin writes: “I don’t recall the NAR [National Association of Realtors] concerning themselves with real estate brokers having access to on-line companies therefore cutting the independent mortgage banker and local lender out of the transaction.”
 - Another real estate agent writes: “NAR predicted the doom and gloom many, many years ago when franchise brokerage was in its formative stages. ERA, RE/MAX, Coldwell Banker et al., were all predicted to end ‘mom and pop’ real estate firms. These franchises have come; many have gone or merged with others. And yet still, ‘mom & pop’ brokerage firms continue to survive because of the personal attention. I welcome the competition, and I will continue to survive.”

Many Real Estate Companies Also Support Open Competition and Oppose S. 1839

The real estate industry, like banking and most other industries, is constantly changing. Larger real estate brokerage firms are increasing their market share every time you turn around. In 1990 there were 150,000 residential real estate firms. Today there are about half that many. The large chains are buying up more and more local firms. Today Cendant – which owns Century 21, Coldwell Banker and ERA – has 23 percent of the existing home sales market and has been aggressive in acquiring real estate companies. In some communities a partnership with the local bank may be the only way to compete with the national chains and maintain a local presence. The Internet is playing a bigger and bigger role with customers, allowing them to surf for the perfect home, at the perfect price, financed with the perfect mortgage loan, and covered under the perfect insurance policy – 24 hours a day 365 days a year. More and more real estate services are being combined, including brokerage, insurance and mortgage services that are offered as “one-stop shopping” packages, a subject I will speak to at length below.

In this new, competitive environment, bankers and real estate professionals have much to offer to each other – and to consumers. Banks like mine could provide needed capital, cross-marketing opportunities, and technology to support the growth of local real estate firms. Real estate professionals could provide the personalized services and experience that is their strength. Many real estate companies realize the strengths that both industries bring to the table. They also realize the severe limitations S. 1839 would impose on their ability to joint market, merge, be acquired, or even to buy a bank.

In February of this year, The Realty Alliance – comprised of many of the nation’s largest and most successful independent real estate companies with a total of 62,000 agents – went on record in opposition to NAR’s position. In its letter to NAR, The Realty Alliance stated: “Our members favor and support a fair, free-market environment unbound by legislative restrictions. We find it hypocritical and fundamentally wrong to ask that national bank subsidiaries be barred from real estate brokerage activity, while real estate brokerages operate mortgage banking, insurance and title insurance businesses.... We believe, in fact, that consumers would benefit from the influx of capital that may result from nationally chartered banks entering this arena. We also believe that increased competition from companies of size would benefit consumers by making all of us sharpen our skills and improve the services we provide. In our view, the role of government is not to limit competition, as your legislation would do, but rather to foster a business environment in which consumers benefit from competition. The members of The Realty Alliance look forward to working, and prospering, in such an environment.”

Paul Harrington, president of DeWolfe New England, which is one of the largest real estate firms in the Northeast, summed it up when he said: “We believe that banks ought to be able to compete with us as long as there are safeguards to insure that deposits are not being improperly invested. It would be hypocritical for us to say otherwise because we promote the fact that we offer customers convenience through one-stop shopping.”²

² *The Boston Globe, February 25, 2001*

II. Promoting Free and Fair Competition – The Fundamental Tenet of the Gramm-Leach-Bliley Act

The Gramm-Leach-Bliley Act established a framework for modernizing our financial system. After working on this for the last 20 years, Congress recognized the need for flexibility in the face of a rapidly evolving financial landscape. As Senator Phil Gramm said at the signing ceremony for this Act: “The world changes, and Congress and the laws have to change with it. . . . We have learned that we promote economic growth and we promote stability by having competition and freedom.”

Providing the same opportunities under the same rules and regulations is a key to promoting free and fair competition. In today’s real estate market, it is commonplace for real estate companies, securities firms and insurance companies to provide end-to-end services, including brokerage, mortgages, and insurance. Yet not all financial service players have equal ability to offer these same services. The Gramm-Leach-Bliley Act was designed to address these inequalities. To examine this in detail, this section looks at three key issues: (1) the market reality that real estate firms are already providing banking and other financial services and that the real estate industry is more concentrated than the banking industry; (2) the system established in the Gramm-Leach-Bliley Act to correct disparity in the provision of financial services among providers and thereby promote free and fair competition; and (3) the changing real estate and financial marketplace that demands a flexible regulatory approach to address inequities that exist today and may exist in the future.

Combining Real Estate Brokerage and Banking Services is Not a New or Unusual Activity

As I previously noted at the outset, real estate companies, securities firms, insurance companies, credit unions, savings associations and, in half the states, state-chartered banks can offer real estate services.³ Ironically, the National Association of Realtors is now objecting to the very combinations that their members have undertaken – offering brokerage, mortgage banking, and, often, insurance under one roof.

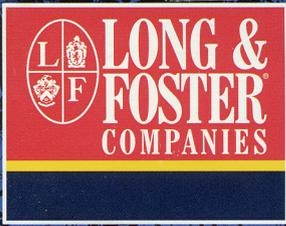
Take, for example, two of the biggest real estate companies in the Washington D.C. area – Weichert and Long & Foster. Both offer the full range of financial services. Weichert calls it “One Stop Gold” and Long & Foster calls it “Real-Edge Services.” These packages provide valuable cost, convenience and service options for customers. These examples show the importance companies – and their customers – place on having the option to combine real estate brokerage, mortgage and insurance services. On the following two pages, I have included several examples of how real estate companies that offer both banking and brokerage services characterize – in their words – their services.

All banks should have the same options. In fact, according to NAR’s own survey in 1999 and a recent 2002 survey by Murray Consulting, not only is one-stop shopping viewed very positively by homebuyers, but banks, mortgage companies and real estate companies are all viewed **equally** as appropriate providers of these services.

Simply put, if real estate services and other financial products are already combined by many real estate and other financial firms, there is no reason why all banking organizations should not be accorded the same opportunities to provide these products to their customers.

In my opening remarks I made the point that this is an issue for banks of all sizes, not just large banks, as NAR has suggested. More than 40 percent of all banks – over 4,000 institutions – have fewer than 25 employees. These are truly small businesses that would like the opportunity to broaden the financial products they can offer their customers and to compete with real estate firms offering loans and homeowners insurance. For the typical community bank, the intent is not to turn real estate brokerage into a major income-producing center, but rather to provide high-quality, high-personal-touch services for customers whose needs the bankers intimately understand and whom they already serve in other capacities. Generally, this is likely to take place by a combination with a local real estate firm – often one that needs the joint effort to compete with the national chains.

³ See attachment developed by the Conference of State Bank Supervisors (CSBS) for a listing of the authorities for each state. Regarding credit unions, recently several credit unions in Wisconsin jointly purchased a majority interest in one of the state’s larger real estate brokerage firms



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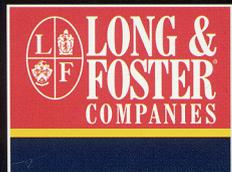
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The nation's oldest real estate company actually started in the **financial arena** nearly 150 years ago, when Baird & Warner began making loans on downtown Chicago properties. We continue to play a dominant role today, with Key Mortgage Services and its subsidiary, North Shore Mortgage, closing more than **\$500 million per year in residential mortgage loans — ranking among the top five mortgage companies** in Illinois. Baird & Warner is once again leading the field, offering the **convenience of “one-stop shopping”** for a wide variety of real estate-related services.

Emphasis added

Source: <http://www.bairdwarner.com/about/default.asp>



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Weichert Financial Services' Weichert Gold Services Program is raising the performance guarantee from \$250 to \$1,000 for all new Gold Services applications. If Weichert Gold Services fails to meet its performance guarantees, the homebuyer will receive a \$1,000 credit towards their mortgage related costs at the time of settlement.*

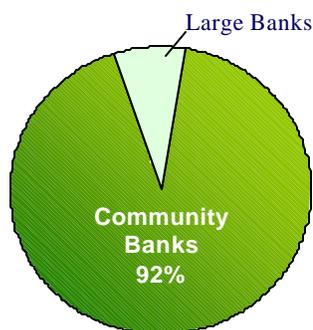
***To participate, the buyer must elect to use Weichert Financial Services to obtain a mortgage, Weichert Insurance Agency to obtain homeowners insurance and Weichert Title Agency or Weichert Closing Services to obtain title insurance.**

Emphasis added

Source: <http://www.weichert.com/>

It is also a misconception that all national banks are large (see Chart 1). In fact, over ninety percent of national banks are community banks. Moreover, of the 10 largest banking firms, four appear to already have the legal authority to engage in real estate activities. There certainly has been no market disruption from the fact that well over half of the insured depository institutions in this country have the ability to offer real estate brokerage and management services today.

Chart 1
Over Ninety Percent of National Banks are Community Banks*



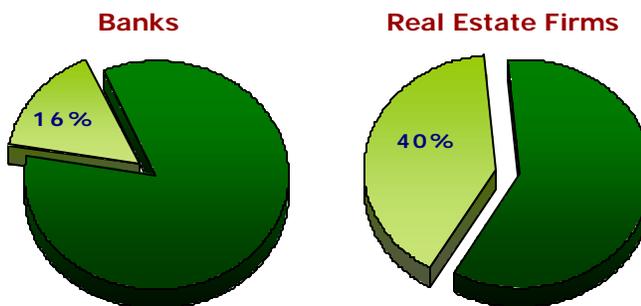
* Defined as banks with less than \$1 billion in assets

Banks that already offer real estate services through the trust department frequently find themselves having to explain to customers that the bank cannot help them with these services outside the trust relationship. These customers do not understand why the bank is unable to do so. Authority to offer real estate services by the banking organization would bridge this unnecessary gap.

What is ironic about NAR's false assertion about large banks wanting to dominate the real estate market, is the fact is that the real estate industry is significantly more concentrated than the banking industry. Today, a few firms dominate the real estate brokerage industry (see Chart 2). In fact, the top **two** firms in the brokerage business (Cendant and RE/MAX) have 33 percent of the market. By comparison, the top **ten** banks have the same 33 percent of the banking market. Cendant Corporation accounts for 1 out of every 4 real estate agents and alone has a 23 percent market share of existing home sales.

Chart 2
The Real Estate Industry is Much More Concentrated than the Banking Industry

■ Market share of top three firms



And because consolidation within the real estate industry is occurring at breakneck speeds, small realty companies are far more likely to be bought up by one of the major real estate firms than by a bank. Many real estate brokers have told the ABA that they would welcome approval of the proposal because it would provide a potential local partner to help them compete with the large national chains. In fact, the local bank can help the small firm, through joint ventures and capital, to compete with the large national real estate firms.

Thus, the marketplace reality is that real estate firms already provide end-to-end services and the largest real estate companies have been increasing their domination over the market.

The GLB Act Was Designed to Allow Flexibility to Adjust to the Marketplace

In the years immediately preceding passage of the GLB Act, Congress recognized that the statutory standard for regulatory approval of new activities for bank holding companies — the “closely related to banking” standard — was woefully inadequate in an economy transformed by technological progress. Thus, Congress agreed to a new, considerably broader, standard to enable banks and bank holding companies to remain competitive no matter in what direction financial services evolved. That new standard — activities that are financial in nature or incidental to a financial activity — was intended to provide the flexibility Congress knew would be necessary. Those activities may be conducted only in financial holding companies (“FHC”) or financial subsidiaries meeting certain safety and soundness and community needs standards enumerated in the statute.

Congress did not give the FRB and the Treasury unfettered discretion to make the determination that an activity is appropriate for approval. GLB Act specifically sets forth certain traditional banking activities that Congress knew were clearly financial in nature.

In addition to these currently-recognized activities, the Act authorizes activities that the FRB and Treasury determine, by regulation or order, to be “financial in nature or incidental to such financial activity.” This authority to permit new financial activities is considerably broader than the

FRB's comparable authority before GLB Act was enacted, which had only extended to a new activity that was "so closely related to banking as to be a proper incident thereto."

One specific aspect of this new authority is that the FRB is directed to define the extent to which three types of activities are "financial in nature:" (1) lending, exchanging, and engaging in certain other transactions with financial assets other than money or securities; (2) providing any device or instrumentality for transferring money or other financial assets; or (3) arranging, effecting, or facilitating financial transactions for the account of third parties. ABA believes the proposed real estate activities qualify under the first and third statutory categories. For example, real estate brokerage is generally the business of negotiating a contract for the purchase, sale, exchange, lease, or rental of real estate – which we believe is a financial asset – for others.

The Fed and Treasury, in their request for public comment, note that many of the essential aspects of real estate brokerage are already permissible under national bank "finder" authority. The regulators already authorize financial holding companies, as well as national banks and their subsidiaries, to act as finders in bringing together buyers and sellers for financial or nonfinancial transactions. Permissible finder activities include "identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction..."⁴ This description of finders authority is the essence of every real estate transaction.

Apart from their authority with respect to these three specified activities, the Fed and Treasury have broad discretion to determine that other types of activities are "financial in nature or incidental to such activity." In making such a determination, the regulators are directed to consider a number of factors. Among the specific factors to be considered are:

- Changes or reasonably expected changes in the marketplace in which financial holding companies compete or the technology for delivering financial services; and

⁴ 12 CFR 7.1002.

- Whether the proposed activity is necessary or appropriate to allow a financial holding company to –
 - Compete effectively with any company seeking to provide financial services;
 - Efficiently deliver information and services that are financial in nature through the use of technology, including applications involving systems for data transmission or financial transactions; and
 - Offer customers any available or emerging technological means for using financial services or for the document imaging of data.

The GLB Act standard is a significant expansion of the Fed and Treasury's capacity to consider the competitive realities of our nation's financial marketplace when determining permissible activities for financial holding companies and financial subsidiaries. It is our contention that the marketplace, and the technology associated with it, in the case of real estate brokerage and property management, have already changed and will continue to change dramatically in ways that significantly impact the ability of banks to effectively compete with other companies that provide financial services.

Finally, in addition to the newly-authorized financial activities described above, the Act authorizes financial holding companies to engage in certain nonfinancial activities. Specifically, a financial holding company may engage in a nonfinancial activity, or acquire a company engaged in a nonfinancial activity, if the Fed and Treasury determine by regulation or order that the activity: (1) is complementary to a financial activity; and (2) does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally.

The NAR would have this Subcommittee believe that Congress meant to preclude real estate activities in the GLB Act and that the legislation accomplished that goal. This is simply untrue, and we have seen no specific evidence to back up this unfounded charge. There is absolutely nothing in the legislative history to support this allegation. To the contrary, the plain language of the statute and the legislative history show the Treasury and Federal Reserve are following exactly the process and using the factors Congress intended.

The GLB Act itself demonstrates Congress's knowledge of this issue in its determination that financial subsidiaries of national banks should be prohibited only from engaging in real estate development activities – the riskier aspect of the business in which the banking organization takes an ownership position. Had Congress intended to prevent banking organizations from engaging in the agency activities of real estate brokerage and real estate management, it clearly knew how to do so. The fact that Congress chose only to prohibit real estate development leads to the conclusion that Congress did not intend to restrict agency activities.

Despite comments to the contrary, anyone who paid attention to the debate over the many years that led up to GLB Act would not have been surprised to see the current proposal. The ABA negotiated with NAR over ten years ago the rules under which banks would enter the real estate brokerage business. This negotiation took place with respect to criteria in a previous version of the GLB Act which was, in fact, much more restrictive than the criteria enacted in 1999. Thus, over ten years ago, the NAR recognized that even a more restrictive version of financial modernization could be interpreted as permitting banking companies to offer real estate brokerage. Furthermore, in 1995, NAR testified on another forerunner of the GLB Act before the House Banking Committee. In that testimony, NAR stated unequivocally that the language must be clarified to exclude brokerage and management. It was not clarified then, nor was it in the GLB Act. That 1995 bill, the "Financial Services Competitiveness Act of 1995," contained similar, but less broad, language to that ultimately enacted in the GLB Act.

Certainly the NAR had every opportunity to raise the issue with Congress in 1999 and either chose not to or did so without success. Rather, NAR's simplistic argument is that the proposal involves "commerce" and is, therefore, beyond the scope of the GLB Act. However, the issue is not at all that simple. The language of the relevant provisions of the GLB Act does not prohibit commercial activities; rather they set out specific criteria to determine permissible activities. The authors clearly recognized that there was no exact or permanent line to define services that should be permissible. That is why they left the determination of whether or not a given activity is financial in nature or incidental to a financial activity to the Fed and Treasury, and why they developed the specific criteria that are in the statute. To reiterate, if Congress had wanted to make such a determination to exclude the proposed activities, it would have explicitly done so – as it did with real estate development.

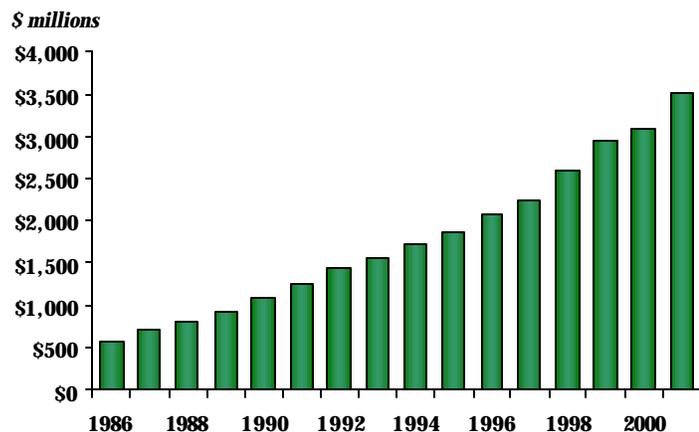
It is worth noting, since NAR has raised the specter of banking and commerce, that the Fed has, for many years, been the primary opponent of breaching the wall between banking and commerce. Based on this record, one would certainly expect the Fed to look very closely at any question relating to commercial activities.

The Changing Real Estate and Financial Marketplaces Require a Flexible Regulatory Approach

As noted above, the GLB Act requires that the regulators consider competitive factors and technological innovations when determining whether activities are financial in nature. A particularly applicable statutory phrase to focus on in this context is whether the activity is “appropriate” to allow institutions to “compete effectively with any company seeking to provide financial services in the U.S.” Other types of insured depository institutions have the authority to provide – and are providing – real estate brokerage and management services. We have already demonstrated that real estate brokerage firms are providing financial services throughout the U.S. Clearly, the fact that real estate brokerage firms are offering mortgages and other financial services must be part of the regulatory consideration. Competitive imbalances like this are the very thing that Congress sought to correct when it enacted the GLB Act, and we believe that the use of the flexibility granted to the regulators under Section 103 (a) is clearly justified in the case of real estate brokerage and management authority for banking organizations.

Technological innovations have also had a dramatic impact on real estate markets. One major change is the development of the secondary market for mortgage loans and the efficient process that bundles individual home loans into highly liquid, globally-traded securities (see Chart 3).

Chart 3
Mortgage Backed Securities Outstanding

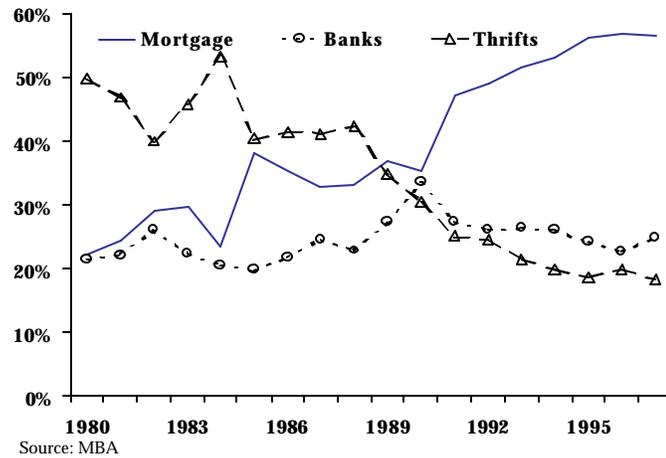


Source: Federal Reserve

Chart 4
Mortgage Originations

The increasing importance of the secondary market has facilitated the rapid growth of mortgage lending outside traditional banking and savings institutions (see Chart 4).

In fact, securitization has significantly changed the very nature of mortgage funding, enabling real estate firms to establish their own mortgage companies and to offer end-to-end real estate transactions – helping a buyer find a home, finance it, and insure it. The result is that traditional deposit-based lenders – banks and thrifts – are often bypassed completely. These are exactly the kinds of technological changes the GLB Act authorized the Treasury and the Fed to address.



The dominance of the secondary market is clear evidence that this form of funding for plain vanilla mortgage loans is generally superior in terms of costs to funding with bank deposits. If banks somehow enjoyed some special benefit from deposits, or deposit insurance (which banks pay for through premiums and extensive regulatory costs), banks would not be selling into the secondary market, and the secondary market would not control an ever-increasing share of the marketplace. No amount of deposit insurance can counteract this fundamental principle of efficient markets. More importantly, access to this secondary market source of funding is available equally to mortgage and banking organizations, and is clearly why real estate companies increasingly are affiliating with mortgage banking companies.

To summarize this section, the GLB Act recognized that achieving the goal of promoting competition necessarily required regulatory flexibility. Section 103 (a) provides that flexibility by authorizing the Fed and the Treasury, subject to certain statutory guidelines, to approve additional activities for banking organizations. The ABA believes strongly that real estate brokerage and management meet the criteria. Of course, the Fed and Treasury have not made any determination

on this proposal. Regardless of their ultimate decision, the Fed and Treasury should be allowed to follow the process Congress created only two and a half years ago.

III. All Consumer Protections Are Maintained and Bank Safety and Soundness Is Protected

If banking organizations offer real estate services, consumers would actually have more protections under the law than they do today. ***All rules applicable to real estate brokers, including all state licensing, qualification and sales practices will apply equally to bank-affiliated real estate agents.***

NAR has raised the specter of customers being taken advantage of as a result of conflicts of interest that may potentially arise when a real estate broker is affiliated with a lender. The simple fact is that the exact same potential for such abuse occurs, for example, each time an agent from Century 21, Coldwell Banker, ERA (all of whom are affiliated with Cendant) GMAC, Long & Foster or USAA helps a customer buy or sell a house. And yet, although these integrated real estate organizations, as well as state banks in many states, savings institutions, and credit unions, have been selling real estate and funding mortgages for years, there has been no outcry about these conflicts of interest. Why? — Because the Real Estate Settlement Procedures Act (“RESPA”)⁵ requires realtors affiliated with lenders to disclose that fact to customers before the purchase occurs.

The RESPA disclosure,⁶ which must be on a separate piece of paper, must state the relationship between the real estate agent and the lender and provide the estimated charges or range of charges of the lender. It must also notify the customer that he or she is *not* required to use the lender and is free to shop around for a better deal. If the real estate agent requires the use of its affiliated lender, that agent violates the kickback and unearned fee provisions of Section 8 of RESPA. The customer is expected to sign an acknowledgement of the disclosure.

⁵ 12 U.S.C. § 2601 *et seq*

In addition, consumers have even more protections when their real estate agent **is** affiliated with a banking organization. This is because banks and bank holding companies and their subsidiaries and affiliates are subject to the anti-tying provisions of the Bank Holding Company Act.⁷ These restrictions prohibit banks and their affiliates from conditioning the provision of credit on the purchase of another product or service.

Another false impression put forward by NAR is that somehow bank involvement is contrary to the spirit of the Community Reinvestment Act. Nothing could be further from the truth. Approval of the proposal would help low income and minority communities. Because banks are subject to CRA, they have every incentive to use the real estate authorities to enhance their outreach to communities. The bank would bring real estate services to areas now shortchanged and could use the combination of real estate and financial services to better serve their low-income and minority communities. Moreover, if the real estate unit were a subsidiary of a national bank, that subsidiary would be covered by CRA.

Bank involvement in real estate brokerage and management services is also consistent with safe and sound banking. First, providing these services will help to diversify the income stream of these institutions and help to improve their financial base. Real estate brokerage and management services are activities where a bank acts only as an agent for a third party, **but does not take an ownership position in the property**. By their very nature, agency activities pose very little risk to the safety and soundness of depository institutions.

Second, under the GLB Act, the bank regulators must deem a bank to be well-capitalized and well-managed before a banking organization can participate in any of the expanded financial activities permitted under the GLB Act, including real estate brokerage and property management. Thus, only financially strong institutions would be authorized to engage in these activities.

⁶ The requirement for affiliated business disclosures is part of the regulations of the Department of Housing and Urban Development that implement RESPA. 24 C.F.R. § 3500.15.

⁷ Section 106(b) of the Bank Holding Company Act Amendments of 1970.

Third, banking organizations are also subject to Sections 23A and 23B of the Federal Reserve Act, which limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Such limits ensure that the safety and soundness of the bank will not be negatively impacted by its subsidiaries or affiliates.

Fourth, many banking organizations already have years of experience in providing real estate activities. In fact, the purchase, sale and management of real estate are frequently significant aspects of fiduciary asset management in many bank trust departments. Because banks currently have trust personnel who provide real estate brokerage and management services on a daily basis to trust customers, providing the service outside of the trust department would not be a new activity in which banking organizations lack expertise. Thus, no new safety and soundness issues would be raised.

Finally, it is important to note that a precedent already exists for bank involvement in real estate activities. In over half of the states, state banking regulators have the authority (either explicitly, through regulatory interpretations, and through wildcard and parity statutes) to allow state-chartered banking organizations to engage in real estate activities (see the attached state-by-state listing developed by the Conference of State Bank Supervisors). Moreover, savings institutions and credit unions already have brokerage authority. Allowing banks the same rights and privileges should enhance the competition for real estate services.

Conclusion

In July, it will be two years since the filing of the original petition requesting a determination that real estate brokerage and management be deemed financial in nature. It is now certain that this determination will not be made until 2003, as was indicated in an April 22, 2002 letter from Treasury Secretary Paul H. O'Neill to Congressman Michael G. Oxley, indicating that, in consultation with the Fed, the Treasury will not make a final decision on this proposed rule until next year.

A fundamental purpose of GLB Act was to enable banking institutions to compete with other financial services providers, and there is ample evidence demonstrating that the real estate competition is touting the advantages of one-stop homebuying services. While we as an industry have always looked at real estate brokerage and management as providing us with more options to compete in the long term, with each passing day, real estate firms become more deeply involved in financial services such as mortgage and insurance, and banks like mine cannot effectively compete for this business. With each passing day, the case for allowing banks to offer real estate services only gets stronger.

As an industry we have grave concerns about the broader effects of this controversy and whether it sets a precedent that could hinder future approvals of new powers under GLB. The Act was designed to keep our financial system up-to-date by delegating those decisions to the Fed and Treasury. This goal is being frustrated by efforts to take the case for determining what is appropriate back to Congress, placing Congress in the very role that it delegated to the agencies with the greatest level of expertise to make these decisions based on specific statutory criteria.

S. 1839 not only frustrates the GLB Act process, it reduces consumer choice. Consumers would have fewer choices of whom to do business with; agents would have fewer choices of whom to work for; and businesses would have fewer choices for joint marketing, fewer potential merger partners, and fewer potential buyers. We believe a competitive market is the best way to provide quality real estate brokerage and management services. Increased competition clearly benefits consumers and the economy. It is a catalyst for innovation, more customer choice, better service, and competitive prices. I have no doubt that my customers and my community would benefit if my small bank could offer these services.

Not only would consumers benefit from bank involvement in real estate services, but also bank involvement is consistent with safe and sound banking. All consumer protections that apply to independent realtors would apply to bank-affiliated real estate agents – plus bank-affiliated agents would be subject to additional anti-tying regulations. And because brokerage and management are agency activities, they pose no financial risk to the safety and soundness of the banking organization.

Just two-and-a-half years ago Congress made the decision to leave this type of determination to the regulators – so that they could keep the financial structure up-to-date and keep Congress out of the middle of competitive disputes. NAR now wants to put Congress back in the uncomfortable position of referee. Congress explicitly gave the Fed and Treasury the flexibility and authority to make these determinations based on their expert knowledge of the changes in the financial services marketplace. Those agencies should be allowed to carry out the authority that Congress wisely provided to them.

I thank you, Mr. Chairman, for this opportunity to present the views of the American Bankers Association.



Real Estate Brokerage

State	Available	Subsidiary Required	Authorization	Citation
Alabama	Yes	No	Statute	5-5A-18
Alaska	No	No	Statute	AS 06.05.272(d)
Arizona	Yes	Yes	Statute	ARS 6-184(A)(7)
Arkansas	No	No	Not Authorized	NA
California	Yes	No	Statute	Cal. Corps. C. Sec. 206 and Cal. Fin. C. Sec. 751.3
Colorado	No	No	Not Authorized	N/A
Connecticut	Yes ¹	Yes ¹	See Footnote ¹	See Footnote ¹
Delaware	Yes	Yes	Statute	Title Five, Delaware Code § 761(a)(3)
DC	Yes ²	NR	NR	NR
Florida	Yes	Yes	Statute	658.67(6), F.S.
Georgia	Yes	No	Statute & Regulation	7-1-261, operational powers of banks; Regulation 80-5-5
Guam				
Hawaii	No ³	No	Wildcard	NR
Idaho	Yes	No	Wildcard	NR
Illinois	No	No	Not Authorized	N/A – Express prohibition exists within IL wildcard statute that grants parity with federal thrifts, among other entities
Indiana	Yes	No	Statute	I.C. 28-1-3.1
Iowa	Yes	No	Statute	Section 524.802
Kansas	No	No	Not Authorized	N/A
Kentucky	No	No	Not Authorized	N/A
Louisiana	No	No	Not Authorized	N/A
Maine	Yes ⁴	No	Regulation	Maine 9B Section 131(6-A); 9B Section 446-A; Regulation #7
Maryland	No	No	Not Authorized	N/A
Massachusetts	Yes	Yes	Statute	G.L.c.167F §2 p. 25
Michigan	Yes	No	Statute	MCL 487.14104(1)
Minnesota	No	No	Statute is Silent	N/A
Mississippi	No	No	Not Authorized	N/A
Missouri	No ⁵	No	Not Authorized	N/A
Montana	No	No	Not Authorized	N/A
Nebraska	Yes	No	Incidental Powers Regulation	Department Statement of Policy #9
Nevada	No	No	Not Authorized	N/A
New Hampshire	Yes ⁶	No	Regulation & Wildcard	Ban 525, Federal Savings Associations Powers
New Jersey	Yes	No	Regulation	NJAC 3:11-11.5(a)(4)
New Mexico	Yes	No	Wildcard	58-1-54
New York	No	No	Not Authorized	N/A
North Carolina	Yes	Yes	Statute	NCGS 53-47c(3)



Real Estate Brokerage					
State	Available		Subsidiary Required	Authorization	Citation
North Dakota	No		No	Not Authorized	N/A
Ohio	No		No	Not Authorized	N/A
Oklahoma	No		No	Not Authorized	N/A
Oregon	No		No	Not Authorized	N/A
Pennsylvania	Yes		No	Parity Statute	7P.S. §201
Puerto Rico	No		No	Not Authorized	N/A
Rhode Island	No		No	Not Authorized	N/A
South Dakota	Yes		No	Interpretation	51-A-2-14(3)
Tennessee	Yes		No	Statute, Regulation & Wildcard	T.C.A. § 45-2-607(d); Regulation Chpt. 0180-19; 45-14-105
Texas	Yes		No - Preferred	Statute	Texas Real Estate License Act
Utah	No		No	Not Authorized	N/A
Vermont	No		No	Not Authorized	N/A
Virginia	No		No	Not Authorized	N/A
Washington	Yes ⁷		No	Wildcard Authority	RCW 30.04.127
West Virginia	No		No	Not Authorized	N/A
Wisconsin	Yes		No	Statute & Regulation	221.0322 & DFI -Bkg#16
Wyoming	Yes		No	Statute	W.S.13-2-101(a)(xiii) & W.S.13-2-101(a)(xii)
SUMMARY	Yes	No	Yes	No	
	26	25	6	45	

NR: Not Reported.

N/A: Not Applicable.

¹ The activity is permissible through a subsidiary. It may also be conducted directly under the authority provided by the "closely related activities" statute [Sect 36a-250(a)(40) of CT General Statutes] or "wild card" statute [Sect. 36a-250(a)(41) of the CT General Statutes]. To date, The Department has not formally acted on any request to conduct the activity.

² The DC Office of Banking & Financial Institutions is presently modernizing its bank, mortgage banking, trusts, savings and loan, and credit union statutes, regulations and chartering requirements.

³ Real estate brokerage is expressly prohibited by state law, unless otherwise allowed through wildcard authority because the activity is permissible for national banks.

⁴ The Department would review on a case-by-case basis and refer to Sections 416 and 419-A of the Maine Banking Statute, together with Regulation 7.

⁵ Depository Trust Companies have real estate brokerage powers under 362.105

⁶ Effective March 16, 2001, Ban 525 allows commercial banks, trust institutions and savings banks to engage in activities and make any investment in the same manner and to the same extent that the activity is permissible for federal savings associations.

⁷ See also the following: Pursuant to RCW 30.04.215(3), 32.08.140(16) and 32.08.146, banks can perform the same activities federal banks can, provided that the activities are approved by the Director of the Department of Financial Institutions.

NOTE: The data included in this table is provided for information purposes only. It should not be construed to be legal guidance.

January 16, 2002

To the Members of the United States House of Representatives:

The Financial Services Coordinating Council (FSCC) in an alliance of the principal trade organizations in each of the financial service sectors formed to address issues that cut across financial industry lines. Its members, the American Bankers Association, the American Council of Life Insurers, the American Insurance Association, and the Securities Industry Association, wish to express their opposition to H.R. 3424.

The fundamental purpose of the Gramm-Leach-Bliley Act (GLBA) was to develop a flexible structure for our financial system that could adjust to changes in technology and other aspects of the marketplace. Congress believed, and we agree, that such a flexible structure would increase the soundness of our financial system, promote economic growth, decrease costs, and provide consumers and businesses with more choices. Congress recognized that the legislative process is too slow to keep pace with changes in technology and the global marketplace, as demonstrated by the long history of Congressional gridlock prior to GLBA.

Congress expressly gave the Federal Reserve Board and Treasury the authority to authorize financial holding companies to engage in new activities in addition to the products and services enumerated in the statute. In delegating this authority, Congress sought to empower experienced and independent financial regulators to make such determinations, based upon elaborate statutory criteria, that match marketplace realities. This is what financial modernization legislation is about: the ability to evolve. H.R. 3424 seeks to return to the pre-GLBA environment where industry competitors ask Congress to choose winners and losers.

The financial services industry, the regulatory agencies, and Treasury are in the very beginnings of interpreting GLBA. Reopening one of its most central provisions would raise a great deal of uncertainty within the industry. We therefore strongly oppose H.R. 3424.

Sincerely,

American Bankers Association
American Council of Life Insurers
American Insurance Association
Securities Industry Association