The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994: Responding to Global Competition

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ARTICLES

THE RIEGLE-NEAL INTERSTATE BANKING AND BRANCHING EFFICIENCY ACT OF 1994: RESPONDING TO GLOBAL COMPETITION

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I. INTRODUCTION

On September 29, 1994, President Clinton signed into law the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. This historic banking legislation allows the formation of larger banks with extensive interstate branch networks by eliminating many of the geographic restrictions currently placed on banks. This will result in a more efficient banking system in the United States which will ultimately enhance the competitiveness of U.S. banks and companies. President Clinton, in signing the bill, described it as one component of a comprehensive strategy developed by his Administration to systematically address the problems of the American economy. Two Chief Executive Officers of major banks who spoke at the September signing ceremony described the legislation as "landmark" and predicted it would help make the United States a stronger competitor in world markets. One characterized it as one of the most significant pieces of banking legislation in our history.

This article will: (1) trace the development of geographic restrictions on the U.S. banking system; (2) recount recent Congressional attempts to remove these restrictions; and, (3) explain the main provisions of the Riegle-Neal bill.

II. THE HISTORY OF GEOGRAPHIC RESTRICTIONS ON U.S. BANKS

American banking has historically been characterized by geographic restrictions—both intrastate and interstate. Such restrictions have been based in part on the fear of excessive concentration of financial power, the desire to promote close relationships between bankers and borrowers, and the aspirations of communities to control

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3. Id.
4. Id.
their economic development. As a result of these restrictions, the U.S. banking system is composed of thousands of independently chartered banks. This contrasts sharply with the highly concentrated banking systems of many European countries, Japan, and Canada. For example, in 1990, the United States had 12,500 insured banks, while Canada had only eight major banks.

A. History of Bank Branching

Before the Civil War bank branching in this country was limited. Most banks were state banks specifically chartered by state legislatures. Branching rights frequently varied from bank to bank in accordance with a particular bank’s charter, rather than from state to state. The First and Second Banks of the United States, which were headquartered in Philadelphia and combined commercial banking with some central banking functions, operated branch offices throughout the country.

In 1836, after President Jackson’s veto of legislation to recharter the Second National Bank, the chartering of banks in the U.S. became exclusively a matter of state law. Each state chartered its own banks and no state provided a general method for the entry of banks chartered by other states. The primary concern during this period was keeping local economies free of financial control by the monied interests in large cities. This led to the establishment of relatively small, locally-oriented banks. The rise of “free banking” in the period immediately before the Civil War contributed to this trend. Under “free banking” laws, no specific legislative charter was required. Rather, anyone meeting specified, minimal statutory requirements (such as initial capitalization) could obtain a charter. Free banks were for the most part chartered as “unit banks”—that is they had no branches.

In 1864, Congress passed the National Banking Act which established a national banking system, and thus laid the foundation for today’s dual banking system. From this point forward, banks could choose to be either chartered as state banks and regulated by state governments or chartered as national banks and regulated by the federal government. Under the Act, national banks did not have the right to branch.

During the late 1880s, interest developed in permitting national banks branch as a means of making banking services available to rural areas that could not support separately incorporated banks. Owners of existing banks, however, were opposed to this idea. Therefore, Congress, in the Currency Act of 1890, reduced the capital required to establish national banks from $50,000 to $25,000 for towns with populations of less than 3,000. As a result, there was a rapid increase in the number of banks, from 13,000 in 1890 to 25,000 in 1910. This growth in the number of banks strengthened an


already powerful anti-branching lobby.\textsuperscript{11}

In the early 1900s, a number of states granted branching powers to their state-chartered institutions, thus providing state banks a competitive advantage over national banks operating in those markets. Some national banks began converting to state charters in order to take advantage of the more favorable branching laws. In the early 1920s, the Comptroller of the Currency attempted to address this competitive imbalance by allowing national banks to branch, but this action was struck down by the Supreme Court in \textit{First National Bank in St. Louis v. State of Missouri}.\textsuperscript{12} The Court held that the National Banking Act did not allow national banks to establish branch offices. Congress acted to protect the national bank charter by passing the McFadden Act in 1927. This Act authorized a national bank to open a limited number of branches in its local community if the law of that state permitted banks chartered by such state to do so.\textsuperscript{13}

The collapse of the U.S. economy in the late 1920s and early 1930s caused extensive bank failures and revealed the weaknesses of unit banking. Consequently, many states enacted legislation to permit their state-chartered banks to branch intrastate. Congress responded in 1933 by amending the McFadden Act to permit national banks to branch throughout their home state to the same extent that the state permitted its own banks to branch. Hence, Congress assigned to state legislatures the power to control national bank branching.\textsuperscript{14}

Even as amended in 1933, however, the McFadden Act did not permit national banks and state banks that are members of the Federal Reserve System to branch into states in which they were not located, regardless of whether state banks were authorized to do so.\textsuperscript{15} Because the McFadden Act does not apply to state-chartered banks that are not members of the Federal Reserve System . . . such banks were allowed to establish interstate branch networks in a state if that state permitted such action.\textsuperscript{16} At present, interstate branching is severely limited. Alaska, Nevada, New York, North Carolina, Oregon, and Rhode Island are the only states that allow interstate branching by state banks that are not members of the Federal Reserve System. Furthermore, each of these states' statutes require reciprocity by the state that headquarters the bank seeking entry.\textsuperscript{17}

\textbf{B. History of Interstate Banking}

In order to avoid the branching restrictions imposed by federal and state governments, banks began to form bank holding companies in the 1940s and 1950s.\textsuperscript{18} "The holding company structure enabled a bank to obtain a rough equivalent to a branch bank even when branch banking itself was impermissible. A holding company could purchase banks in different localities both within and outside a state."\textsuperscript{19} Originally,
most holding companies were created in an effort to expand geographically in what were otherwise unit banking states.

1. The Douglas Amendment

The bank holding company structure did not impart all the efficiencies of branch banking, but it did allow banks to expand the geographic scope of their operations. This so-called loophole around interstate banking restrictions was partially closed by the Douglas Amendment of the Bank Holding Company Act of 1956. The Douglas Amendment applied the principles of the McFadden Act to the bank holding company structure. It prohibited the interstate acquisition of a bank by a bank holding company unless explicitly authorized by a statute of the state where the bank to be acquired was located.

In 1978, out-of-state bank holding companies to acquire Maine banks. The legislation was motivated in large measure by Maine’s desire to attract new investment capital. The law initially required reciprocity. In other words, bank holding companies headquartered in another state, New York for example, could acquire Maine banks only if bank holding companies headquartered in Maine were allowed to acquire New York banks. Because of the reciprocity requirement no acquisitions of Maine banks were possible until other states enacted statutes allowing the acquisition of their banks by Maine bank holding companies.

Other interstate banking statutes were enacted in the early 1980s, with Alaska, Massachusetts, and New York passing laws that became effective in 1982. In general, state statutes allowing out-of-state bank holding companies to acquire banks within a state imposed two types of restrictions on out-of-state bank holding companies—regional restrictions and reciprocity restrictions. Reciprocity restrictions are described above. Regional restrictions required the acquiring bank to be located within the same region of the country as the bank to be acquired. Many states enacted laws imposing both types of restrictions on out-of-state institutions.

2. Regional Compacts

In 1982, Massachusetts started the movement toward regional interstate banking arrangements by passing

a law permitting a bank holding company whose principal place of business was located in Connecticut, Maine, New Hampshire, Rhode Island, or Vermont to acquire a bank or a bank holding company in Massachusetts. The law, however, permitted such acquisitions only if the state in which the acquiring bank was located expressly authorized similar acquisitions by a Massachusetts holding company under conditions no more restrictive than those imposed by the Massachusetts law.

20. Id.
22. Nestor, supra note 14, at 619.
25. Id.
Connecticut followed the Massachusetts lead and enacted a similar law in 1983.27

The regional compact created by Massachusetts and Connecticut was challenged in the courts because it did not provide equal entry rights for banks headquartered in all states. The challenge was based on the grounds that the Douglas Amendment did not authorize regional compacts and that by discriminating against non-New England banks the compact violated the Commerce and Equal Protection clauses of the Constitution. The United States Supreme Court upheld the regional laws in June 1985 in Northeast Bancorp v. Board of Governors of the Federal Reserve System.28 The Court stated that the legislative history of the Douglas Amendment, including its strong analogy to the McFadden Act, led to "no other conclusion but that Congress contemplated that some states might partially lift the ban on interstate banking without opening themselves up to interstate banking from everywhere in the Nation."29 Based on the Supreme Court's decision in Northeast Bancorp, many states have enacted some form of interstate banking legislation. Today, a majority of states allow for full, nationwide interstate banking, but many states continue to impose restrictions on acquisitions. At present, 34 states permit nationwide interstate banking, 15 states and the District of Columbia permit interstate banking acquisitions on a regional basis, and only one state, Hawaii, permits no interstate banking.30

III. CONGRESSIONAL ATTEMPTS TO REMOVE GEOGRAPHIC RESTRICTIONS ON BANKING AND BRANCHING IN THE U.S.

A. Congress Commissions a Presidential Report

After enactment of the Bank Holding Company Act in 1956, Congress took no action on interstate banking and branching for two decades. However, in the late 1970s, American banks complained that foreign banks operating in the U.S. had a competitive advantage. Foreign banks were not restricted by the McFadden Act, and thus were able to establish interstate branch networks. In 1978, Congress passed the International Banking Act which, among other things, restricted foreign bank branching privileges and for the first time established federal rules to govern foreign bank operations in the United States. This Act established a national treatment standard to create a level playing field for domestic and foreign banks.31

In that 1978 Act, Congress also asked the President to submit a report on the applicability of U.S. banking laws to current banking conditions. The report, delivered to Congress during the closing days of the Carter Administration in January 1981, examined the impact of both the McFadden Act and the Douglas Amendment on U.S.

27. Nestor, supra note 14, at 622.
29. Id. at 172.
banks. It concluded that the geographic restrictions imposed by these laws were increasingly "ineffective, inequitable, inefficient, and anachronistic" and recommended that "interstate banking be ratified and further liberalized through a phased relaxation of current geographic restraints." It concluded that the geographic restrictions imposed by these laws were increasingly "ineffective, inequitable, inefficient, and anachronistic" and recommended that "interstate banking be ratified and further liberalized through a phased relaxation of current geographic restraints."
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tually non-stop on the issue and presented the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) to the President to sign in August 1989.\textsuperscript{39}

Despite the savings and loan crisis and the intensity with which the Senate Banking Committee worked to resolve it, Chairman Riegle took time on July 11, 1989, to hold the first of over 40 hearings during his six year tenure as Chairman on the competitiveness of the U.S. in today’s global economy. Senator Riegle’s home state of Michigan was devastated during the 1970s and 1980s by the automobile industry’s loss of market share to foreign imports. He was thus acutely aware of the competitive challenges the increasing globalization of international markets posed for the American economy. In his opening statement at the July 11 hearing, the Chairman expressed his concerns:

There is no issue that is more important to this Senator than the competitiveness of all sectors of our economy in today’s global environment. This topic will be a dominant theme of the period of time of my chairmanship and it is my intention to hold a comprehensive series of hearings on these issues . . . . Over the years I have become increasingly concerned . . . about the ability of the United States to compete effectively in the international marketplace. This has serious ramifications not only for our standard of living, but clearly for our national defense and long term economic and military security.\textsuperscript{40}

As a result of these concerns, Congress included a provision in FIRREA directing the Secretary of the Treasury to review the U.S. financial system and submit a comprehensive reform proposal by February 1991.\textsuperscript{41} Chairman Riegle, in order to prepare the Senate Banking Committee to deal with the major reform proposals it would be receiving in 1991, scheduled a series of 13 hearings to examine options for federal deposit insurance reform, as well as broader financial modernization measures to make U.S. banks more competitive. At the hearings, numerous industry and government representatives expressed serious concerns about the competitive decline of our financial institutions. The Chief Executive Officer of Chase Manhattan Bank, speaking on behalf of the American Bankers Association (ABA), told the Committee that our banks were losing their competitive edge in international financial markets, and that this would reduce the competitiveness and market share of other U.S. industries, especially export-related industries.\textsuperscript{42} Gerald Corrigan, the President of the Federal Reserve Bank of New York, testified that American banks were in competitive decline which threatened the leadership position of the United States in world financial markets. He listed several factors causing the decline, among them “an outdated legal institutional framework” including the McFadden Act and the Douglas Amendment to the Bank

\begin{thebibliography}{99}
\bibitem{40} \textit{Oversight Hearings on the Condition of U.S. Financial and Industrial Base: Hearings Before the Senate Comm. on Banking, Housing, & Urb. Aff.}, 101st Cong., 1st Sess. 1-2 (1989); Senator John Heinz [R-PA], the number two Republican on the Committee, shared Chairman Riegle’s concerns. He noted that other foreign governments had consciously adopted strategies to ensure the competitiveness of their key industries.
\bibitem{42} \textit{Financial Modernization Hearings} (1990), \textit{supra} note 38, pt. I, at 63.
\end{thebibliography}
Holding Company Act.\textsuperscript{41} In addition, Chairman of the Federal Reserve Board Alan Greenspan\textsuperscript{42} and FDIC Chairman William Seidman strongly recommended removing the restrictions on interstate banking and branching as a means of strengthening the competitiveness of U.S. banks.\textsuperscript{43}

In June 1990, several representatives of foreign financial institutions also testified, including top officials from Germany’s Deutsche Bank, England’s Barclays Bank, and Japan’s Fuji Bank. The European official informed Committee members that the European Community’s Second Banking Coordination directive, adopted as part of a series of measures to strengthen the competitiveness of European economies, would let European banks branch across the European continent.\textsuperscript{44} Every witness told the Committee that American banks were handicapped by domestic geographic restrictions which prevented them from building a strong home base for their international operations.\textsuperscript{45} These witnesses also told the Committee that geographic restraints made U.S. banks less stable because they could not diversify their loan portfolios across regions and industrial sectors.\textsuperscript{46} Later that summer, Secretary of the Treasury Nicholas Brady testified before the Committee and expressed similar views to those of the other witnesses. He went even further, however, to point out that the European Communities’ decision to provide universal banking powers on a continent-wide basis would greatly improve the competitiveness of European banks.\textsuperscript{47} and, therefore, could handicap the competitiveness of U.S. banks if geographic restrictions on interstate banking and branching in this country were not eliminated.\textsuperscript{48}

D. Failed Attempt in 1991

On February 5, 1991, the Administration submitted its report “Modernizing the Financial System” to the Congress which recommended fundamental reforms to ensure a safer, more competitive banking system, including legislative changes to the McFadden Act and the Douglas Amendment of the Bank Holding Company Act that would permit nationwide banking and branching. The Report also called for repeal of the Glass-Steagall Act—which separates traditional commercial banking from investment banking—and prohibits commercial affiliations with banking organizations.\textsuperscript{49}
The report noted that U.S. banks were losing market share at home to foreign banks and other financial institutions as well as abroad to foreign banks. It noted:

As recently as 1983, three U.S. commercial banks were among the world’s top twenty in asset size; by year-end 1988 no U.S. bank was ranked among the world’s top twenty. In addition of the world’s top 50 banks in market capitalization in 1988, only two were U.S. banks.2

President Bush emphasized the importance of financial reform in his State of the Union Address3 and in his letter to Congress transmitting his 1991 Economic Report. In that letter, he wrote that “lifting restrictions on interstate banking activities and on the ability of banks to combine with commercial and other financial firms will increase banks’ competitiveness.”4

On March 5, 1991, Chairman Riegle introduced a bill—S. 543, the Comprehensive Deposit Insurance Reform and Taxpayer Protection Act of 1991—to reform the deposit insurance system. The Committee held numerous hearings on both the Administration’s proposal and S. 543. Chairman Riegle’s bill as introduced did not contain any provisions on interstate banking and branching. However, after a March 20, 1991, hearing on the Administration’s interstate banking and branching proposals, Chairman Riegle worked with Senator Dodd [D-CT] and other interested Committee members to develop acceptable provisions. The Administration’s interstate banking and branching proposal did not have wide support on the Committee because it failed to address concerns about concentration and did not provide an adequate role for states in controlling branching of out-of-state banks. In addition, it did not provide states with the ability to “opt-out” of interstate branching, a concept which was introduced by Senator Dodd in his 1990 interstate banking bill, S. 2922.5 The Committee began marking up S. 543 as modified by the Chairman and other fellow senators on July 31, 1991.6 Committee members considered this comprehensive legislation for three days. On August 2, 1991, the Senate Banking Committee reported out S. 543 as amended during the three-day markup by a vote of 12 to 9. For the first time, the Committee had reported legislation to remove the restrictions on interstate banking and branching. The bill permitted, among other things, bank holding companies that are adequately capitalized and managed to: (1) after one year acquire existing banks in any state, subject to concentration limits; (2) after two years establish subsidiary banks in any state; and, (3) after three years convert subsidiaries into branches of the main bank, or establish de novo branches, unless a state passed legislation to opt-out of interstate

background of these provisions and an explanation of the Bush Administration’s effort to repeal it, see REP. DEPT TREASURY (1991), supra note 6, at xviii. In August of 1991, the Senate Banking Committee debated S. 543 which then contained provisions to repeal the Glass-Steagall Act. Those provisions, however, were deleted before the bill was taken up by the full Senate in November of 1991. See S. Rep. No. 167 (1991), supra note 5, at 147.

52. REP. DEPT TREASURY (1991), supra note 6, at 7-8.
56. A mark-up is when members of a Committee meet, at the invitation of the Chairman, to consider and amend bills he or she presents to them. When a bill has been marked up, it is reported by the Committee. Committee staff then writes a report which accompanies the bill and is filed prior to the bill’s consideration by the full Senate. STANDING RULES OF THE SENATE, Rule XXVI(10)(b).
branching. During November 1991, the Senate debated the interstate banking and branching provisions of S. 543, and on November 14 adopted an amendment offered by Senator Ford [D-KY] to modify the provisions reported by the Banking Committee. On November 21, 1991, the Senate passed S. 543 by voice vote and became the first body of Congress to remove the geographic restraints on interstate banking and branching. No such provisions were contained in the reform bill passed by the House. A conference committee, impaneled to reconcile differences in the respective House and Senate bills, failed to include the interstate branching provisions found in the Senate version. Chairman Riegle later revealed that Congressman Dingell [D-MI], the Chairman of the House Energy and Commerce Committee, wanted to impose new restrictions on banks' securities powers as a quid pro quo for accepting the interstate banking and branching provisions. Secretary of the Treasury Brady refused to agree to this and, therefore, the interstate banking and branching provisions were not included in the legislation approved by conferees.

In 1992, Senators Dodd [D-CT], Sanford [D-NC], Kerry [D-MA], D'Amato [R-NY], and Garn [R-UT] introduced S. 2207, an interstate banking and branching bill very similar to that passed by the Senate in 1991. A similar bill, H.R.4170, was introduced in the House in 1992 by Congressmen Vento [D-MN] and Wylie [R-OH]. However, no action was taken on these bills because it was a Presidential election year, a time when members do not want to take up controversial legislation.

E. Action in the 103d Congress

On February 16, 1993, Senator Dodd introduced S. 371, a bill to permit interstate banking that was fashioned on the provisions of S. 543 as reported by the Senate Banking Committee in 1991. Two months later, on April 22, Senator Ford introduced S. 810, an interstate banking bill that was similar to the interstate banking and branching bill passed by the Senate in 1991. Both bills permitted: (1) bank holding companies to turn existing subsidiary banks into branches of the main bank; (2) banks to branch interstate by purchasing and converting banks into branches of the main bank; and, (3) banks to opt-out of interstate branching. The principle difference between the two bills involved de novo interstate branching. Under the Ford bill, a state had to pass a statute authorizing de novo interstate branching, while Dodd's bill did

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57. S. REP. NO. 167 (1991), supra note 5, at 61. The version of S. 543 marked up by the Committee amended both the McFadden Act and the Douglas Amendment to the Bank Holding Company Act.
58. S. REP. NO. 240 (1994), supra note 7, at 3. Senator Ford's amendment, among other things, eliminated the provisions for de novo branching and also modified the Committee's proposed treatment of branches of foreign banks.
60. Transcript of Mark Up on S. 1527, The Fair Trade in Financial Services Act of 1993, Senate Comm. on Banking, Housing, & Urb. Aff., 103d Cong., 2d Sess. 15 (1993) [hereinafter cited as Transcript (1993)]. Chairman Dingell, although a conferee on other portions of the conference to reconcile S. 543 and H.R. 3768, was not a conferee on the interstate banking and branching provisions. Due to his forceful personality, other House conferees and Speaker Foley [D-WA] were reluctant to cross him on matters of importance to him. Congressman Dingell refused to accept interstate banking and branching without a deal to restrict banks' abilities to sell securities.
61. See generally Financial Modernization Hearings (1990), supra note 38.
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not require any state action—de novo interstate branching was deemed permissible. Bankers favored the Ford version as it enhanced the franchise value of existing banks.

The Committee held hearings on October 5 and November 3, 1993, on Title III of S. 543, the interstate banking and branching provisions passed by the Senate in 1991. Witnesses were also invited to testify concerning Section 704 of S. 543, the provision that dealt with the insurance activities of national banks. At the October hearing, the representative of the American Bankers Association (ABA) declared support for the interstate banking provisions passed by the Senate in 1991, but expressed strong opposition to any effort to restrict the sale of insurance by banks. Furthermore, the ABA threatened to block passage of an interstate banking and branching bill that restricted bank insurance powers.

In an October 25, 1993, speech outlining the Clinton Administration’s banking agenda, Secretary of the Treasury Bentsen called on Congress to remove the geographic restrictions to interstate banking and branching. He stated, “We currently have a de facto system of interstate banking, but it’s a patchwork system, and it’s clumsy.” Under Secretary of the Treasury Frank Newman, at the Committee’s November 3 hearing, announced support generally for the principles of the interstate banking and branching provisions passed by the Senate in 1991.

F. Insurance Amendment Delays Markup

Chairman Riegle scheduled a markup for November 18, 1993, on a Committee Print embodying the interstate banking and branching provisions of S. 543. Prior to the markup, Senator Dodd filed an amendment to restrict the insurance activities of banks. His amendment closely resembled Section 704 of S. 543 as passed by the Senate in 1991. The banks lobbied against the amendment. Many members of the Committee did not want to have to vote on the issue. As a result, a quorum could not be established and the Committee could not proceed with the markup. Senator Dodd declared that he

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64. Letter from Sen. Donald W. Riegle, Jr. to Under Secretary of the Treasury Frank Newman (Sep. 23, 1993) (invitation to testify). Section 92 of the National Bank Act, enacted in 1916, authorizes a national bank located in a town with a population of 5,000 or less to sell insurance, subject to the regulations of the Comptroller of the Currency. While the legislative history of this provision is not extensive, it apparently was intended to promote availability of banking services in rural areas by allowing small-town banks to sell insurance, thereby enhancing the financial viability of such banks.

In 1986, the Comptroller interpreted this provision to permit a national bank or branch in a town of 5,000 to sell insurance nationwide. Some states have prohibited banks and bank affiliates from selling insurance. The Comptroller’s 1986 action, however, preempted such state laws.

In 1991, the Senate passed legislation overturning the Comptroller’s 1986 decision. Section 704 of S. 543 passed by the Senate on November 21, 1991, would have repealed the town of 5,000 provision altogether. It would have allowed a national bank in a town of 5,000 or less to sell insurance only to individuals living and working in, and businesses located in, the town and contiguous rural areas within 7.5 miles. Neither Section 704, nor similar measures passed by Committees of the House of Representatives, were included in the banking legislation passed by Congress in 1991.

In July 1993, in Independent Insurance Agents v. Ludwig, 997 F.2d 958 (D.C. Cir. 1993), the Court of Appeals for the District of Columbia upheld the Comptroller’s interpretation of Section 92. This vastly strengthened the bargaining leverage of the banks on insurance issues. They would no longer accept the language they agreed to in Section 704 of the 1991 bill that passed the Senate.


would not let an interstate banking bill be reported out of Committee without a vote on his amendment.\textsuperscript{68}

On February 3, 1994, the House Banking Committee's Subcommittee on Financial Institutions Supervision, Regulation and Deposit Insurance approved interstate banking and branching legislation by a unanimous vote of 29-0. Movement on interstate banking and branching seemed stalled in the Senate when, that afternoon, Senator Dodd went to the Senate floor to make a major announcement on the subject. He told the Senate:

I have been for years concerned about the sale of insurance products by our nation's banks. Over the past two years banks have dramatically expanded their insurance sales activities. This has occurred not as a result of sound policy choices by Congress, but rather as a result of creative legal interpretations by federal bank regulatory agencies... For several months I have been working with a number of banks, insurance agents groups and insurance companies to craft a reasonable amendment to deal with this matter.\textsuperscript{69}

Senator Dodd then announced any such amendment did not have the "horsepower" to move beyond the Committee. He said, "I do not want to compromise interstate legislation by linking these two issues, which I think would defeat or severely slow down the... legislation." He went on to announce that he would not offer an insurance amendment during any Committee mark up of interstate legislation.\textsuperscript{70}

G. With Insurance Issue Removed, the Path Clears

Following this announcement, the Committee held a markup on the Chairman's Committee Print on February 23, 1993. Senator D'Amato [R-NY], the ranking Republican on the Banking Committee, urged his colleagues to support the Riegle Committee Print "because it is the first step toward making the U.S. a more competitive force in the global financial services marketplace."\textsuperscript{71} At the markup, Senator Gramm [R-TX] told Chairman Riegle, "It's a very good bill. I hope it becomes law. I think it will be part of your legacy as Chairman."\textsuperscript{72} It was reported out of the Committee by a vote of 19-0 and was then introduced as an original bill, S. 1963, by Chairman Riegle on March 23, 1994. The House passed an interstate banking and branching bill, H.R. 3841, on March 22, 1994.\textsuperscript{73}

Majority Leader Mitchell granted the Senate Banking Committee floor time to take up S. 1963 on April 25, 1994. When Chairman Riegle presented the bill to the full Senate that day he told Senators:

The restrictions on interstate branching are an American anomaly. The United States is the only industrial country that restricts bank branching. The globalization of the U.S. banking industry means that U.S. banks cannot afford to continue to base their success on a limited geographical area. They cannot match their competitors while burdened with costly subsidiary structures and cannot be strong global
competitors without larger deposit bases in this country. Removing the restrictions on bank branching will permit American banks to become strong global competitors with an enhanced capacity to help U.S. companies sell their goods in markets abroad.74

Senator Murkowski [R-AK], who was not a member of the Banking Committee, took the floor to announce his support for S. 1963, noting it would help our banks compete with their international counterparts.75 Senator Ford, who was also not a member of the Banking Committee, claimed that the interstate bill passed by the House gave foreign banks competitive advantages and urged Senate Conferees to rectify that in Conference.76 On April 26, after the Senate passed S. 1963 by voice vote, it took up H.R.3841, stripped it of all but its enacting clause, substituted the text of S. 1963, and sent it to the House asking for a conference to reconcile the differing provisions.77

H. A New Obstacle to Passage

Conferees from the two bodies did not meet for three months as House and Senate staff worked to resolve most of the more than 40 differences between the House and Senate bills, many of which were both complex and technical. On July 25, 1994, Conferees met and quickly accepted the staff recommended resolutions.78 They then spent a considerable amount of time discussing an item that had not been present in either bill. This was the so-called homestead provision brought in to the Conference by Congressman Gonzalez [D-TX], the Chairman of the House Banking Committee. After passage of the House interstate bill in March, the U.S. Court of Appeals for the Fifth Circuit upheld a regulation issued by the Office of Thrift Supervision that preempted a provision of the Texas Constitution protecting homesteads of Texas borrowers from foreclosure on loans using the homestead as collateral unless such loans were made for the purpose of purchasing or improving the property.79

Chairman Gonzalez, being from Texas, was unhappy that the Fifth Circuit upheld the preemption of the Texas Constitution by a federal regulation. He was determined to use the interstate bill as a means of overturning the court decision, and made it clear there would be no bill if he was not satisfied on this point. On the other hand, his Texas colleague Senator Gramm argued against Senate acceptance of the Gonzalez proposal, and when outvoted told the conferees he would raise a point of order against the Conference Report on the basis it violated Rule XXVIII(2) of the Standing Rules of the Senate which bars conferees from inserting in Conference Reports matters not passed by either body. Chairman Riegle argued that the homestead provision was a consumer protection amendment and was, therefore, relevant to other consumer protection provisions in the bill. He asserted his belief that the Senate Parliamentarian would rule against Senator Gramm’s point of order.80

77. 140 CONG. REC. S4821 (daily ed. Apr. 26, 1994).
79. Id. at 57-58.
80. His belief was based on a passage (Floyd M. Riddick, SENATE PROCEDURE: PRECEDENTS AND
As Conferees were completing their work, Senator Sarbanes [D-MD] saluted Chairman Riegle, who was retiring from the Senate, for his outstanding six year service as Banking Committee Chairman. He moved that "the very important and significant piece of legislation" be named after Senator Riegle. House Conferees agreed and asked that it also be named after Congressman Neal [D-NC], the Chairman of the House Banking Committee's Financial Institutions Subcommittee who had done so much to move the bill through the House. Conferees then approved the Conference Report and it was filed on August 2, 1994. Two days later the full House considered and passed the Conference Report. The Senate was occupied debating President Clinton's health care plan and took its summer recess without acting on the report.

Concerns were raised that when the Senate returned in September it would make an effort to salvage President Clinton's health care reform proposals and the interstate bill would not be given floor time if it looked as if there would be a long floor fight over its passage. Various Senators and institutions interested in the passage of the final bill furiously lobbied Senator Gramm to refrain from filibustering and/or raising a point of order against the Conference Report. Despite Senator Gramm's stated opposition, the Senate Majority Leader scheduled the Conference Report for consideration by the full Senate on September 13, 1994. Senator Gramm refrained from making his point of order and the Conference Report quickly passed the Senate by a vote of 94-4.

President Clinton signed the bill into law on September 29, 1995. Speaking at the ceremony, Thomas LaBreque, the Chief Executive Officer of Chase Manhattan Bank, said passage of the bill "demonstrated a national commitment to making the United States efficient and globally competitive." He told the assembled leaders that, "This law will change that and enable global banks such as Chase to compete more successfully around the world as well." President Clinton agreed and in signing the bill said it fit into his Administration's comprehensive economic strategy to make the country more competitive.

Three weeks later as Chairman Riegle's 18-year Senate career was being completed, Secretary of Commerce Ron Brown wrote to him and said:

I am writing to salute you for the truly outstanding work you have done as Chairman of the Banking Committee over the last six years . . . Among the most important of your legislative achievements were the provisions of the Export Enhancement Act of 1992 requiring the Executive Branch to formulate a competitiveness strategy for our nation and an export promotion strategy. The Riegle-Neal Interstate

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81. Id. at 44.
82. Id. at title page. In an attempt to show sympathy for Sen. Gramm's objection to the inclusion of the homestead provision in the Conference Report, Senate Banking Committee Republicans refused to sign the Conference Report.
84. 140 CONG. REC. S12765-68 (daily ed. Sept. 13, 1994).
86. Id.
Banking and Branching Efficiency Act of 1994 will also strengthen our banking system’s ability to help U.S. exporters. Your Committee’s bipartisan work on this matter has served our nation well and has helped us prepare to meet the global economic challenges of the 21st century.87

Making U.S. banks and the American economy more competitive was not the only reason Congress passed the Riegle-Neal bill. Congress also believed the legislation would promote diversification of banks’ assets and loan portfolios and help banks survive downturns in local economies. This, it was believed, would also help safeguard the taxpayer-backed Bank Insurance Fund.88 Congress also believed the bill would lead to greater customer convenience and enhance choices for consumers. But it is the contention of the authors of this article that a key moving force behind the bill was the conviction that America had to end the geographic restrictions on its banking system to enhance the competitiveness of our banks and economy in general. The authors also believe that resolving this issue will make it easier to deal with product liberalization issues that have also been cited by many as another aspect of strengthening the competitiveness of U.S. banks and our banking system.

IV. MAJOR PROVISIONS OF THE RIEGLE-NEAL BILL

A. Interstate Banking

Section 101 amends Section 3(d) of the Bank Holding Company Act to provide that one year after its enactment (September 30, 1995) a bank holding company, that is adequately capitalized and managed may acquire banks in any state. Unlike Section 102 which governs interstate branching, Section 101 does not allow any state to opt-out of interstate banking. It does preserve state laws which require an acquiring company to purchase a bank that has been in existence for a specified period of time (not to exceed five years). States, however, may not discriminate among out-of-state buyers.

Interstate expansion by bank holding companies is subject to concentration limits. The Federal Reserve Board is prohibited from approving an interstate acquisition that would result in the holding company controlling more than 30 percent of the deposits held by insured depository institutions in a particular state, unless the host state eliminates the limitations entirely or has a lower concentration restriction. The Federal Reserve would also be prohibited from approving an acquisition if, as a result, the bank holding company would control more than 10 percent of the total amount of deposits of insured depository institutions in the United States.89 The concentration limits would not apply to initial entry into a state by a bank holding company. The Act also provides that the concentration limits do not supersede nondiscriminatory antitrust laws, which will continue to govern banking mergers and consolidations as before.

87. Letter from Secretary of Commerce Ron Brown to Chairman Riegle (Oct. 21, 1994).
88. Congress created the Bank Insurance Fund (BIF) in Section 211 of the Financial Institutions Reform Recovery Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, 218 (1989). The BIF is administered by the Federal Deposit Insurance Corporation (FDIC) and is the successor of the FDIC’s previous insurance fund. Section 226 also created the Savings Association Fund Advisory Committee, which is also administered by the FDIC to insure deposits at savings and loan chartered institutions.
89. There is plenty of room for consolidation before any bank will run into this limitation on expansion by acquisition. BankAmerica, which controls the most domestic deposits has less than 4.5% of the total. Paul Simoff, Branching Law Can Pan Out as a Bonanza for Small Banks, AMERICAN BANKER, Oct. 26, 1994, at 8.
Section 101 further provides that the Federal Reserve Board, in acting on any application for an interstate acquisition under Section 3(d) of the Bank Holding Company Act, should consider the applicant's record of compliance with the Community Reinvestment Act of 1977\(^\text{90}\) and with state community reinvestment laws as well.

**B. Interstate Branching**

Section 102 of the bill permits interstate mergers and consolidations of existing banks starting June 1, 1997. Thus, a bank in State A could merge with a bank in State B and the bank in State B could be operated as a branch of the bank in State A. Similarly, an existing network of bank holding company subsidiary banks could be consolidated into branches of a single bank on that date. States can also opt-in to allowing out-of-state banks to acquire branches from an existing bank, rather than purchase the entire bank.

To be eligible to merge interstate each bank involved in the transaction must be adequately capitalized and managed when the application is filed. Thus, a bank holding company with some distressed subsidiaries must recapitalize them before they can be merged. The resulting bank must also be adequately capitalized.

Concentration limits, the same as those for interstate banking, apply to branching and consolidation as do any lower state deposit caps. The concentration limits, however, do not apply to any mergers of banks that are already affiliated. This would allow a bank holding company to consolidate its existing network of subsidiary banks into one bank with branches even when some of the existing subsidiaries have a market share larger than the limits.

States can opt-out of the interstate merger/branching provisions by enacting a law to that effect after the date of enactment (September 29, 1994) and before June 1, 1997. If a state opts-out of the branching provisions, its banks cannot participate in interstate branching in any way. States can also opt-in and allow branching to take place before June 1, 1997. Section 103 of the bill also allows states to opt-in to de novo branching, that is to permit a bank to open an out-of-state branch without merging with an existing institution or acquiring an existing branch. A bank that opens a new branch in a state that opts-in will be subject to all the same conditions that apply to branching by acquisition.

One of the most contentious issues faced by the Senate and House conferees concerned what powers host states would have over the newly-established branches of a national bank headquartered in another state. The Senate bill provided that branches of national banks would be subject to the host state laws as if they were branches of national banks having their main office in the state. The House bill, however, provided that any branch of an out-of-state national bank would be subject to state law with respect to interstate branching, consumer protection, fair lending and community reinvestment as if they were branches of a host state bank, except to the extent that such state law was preempted by federal law on the same subject.

The manner by which these provisions were reconciled was of enormous importance to the Office of the Comptroller of the Currency (OCC), the regulator of national

\(^{90}\) 12 U.S.C. § 2901 (1994). The Office of the Comptroller of the Currency, the regulator of nationally chartered banks, established a framework and criteria by which it would assess whether a bank was meeting the credit needs of its community. New regulations, effective in 1995, specifically include low and moderate income neighborhoods. 12 C.F.R. § 25 (1995).
banks, and the Conference of State Bank Supervisors (CSBS). The OCC wanted to retain his authority to preempt, either by letter or regulation, state laws that interfered with the safe and efficient operation of national banks. The CSBS wanted to ensure the OCC could not lightly preempt state laws of major importance to states. The conferees finally agreed that the laws of the host state regarding community reinvestment, consumer protection (including applicable usury laws), fair lending, and establishment of intrastate branches will apply to any branch of a national bank in the host state to the same extent as such state laws apply to a branch of a bank chartered by that state, except when Federal law preempts, or if the Comptroller determines that the state law has a discriminating effect on the branch in comparison to branches of state chartered banks.\(^9\)

Section 105 of Riegle-Neal permits the appropriate bank supervisor of a host state to examine branches of out-of-state banks to assure compliance with host state laws, including those governing banking, community reinvestment, fair lending, consumer protection and permissible activities, and to assure that the activities of the branch are conducted in a safe and sound manner. State bank supervisors are permitted to enter into cooperative agreements to facilitate supervision of state banks operating interstate.

Section 107 of the bill attempts to meet the concerns that were expressed by Senator Ford during Senate debate of S. 1963 concerning the competitive advantages enjoyed by the wholesale direct branches of foreign banks. Section 107 provides that if a foreign bank buys a U.S. bank and converts it into an uninsured branch of the foreign bank, the branch will continue to be subject to CRA requirements.\(^2\) The Section also tightens regulations that govern the types of deposits of less than $100,000 that may be gathered by uninsured branches of foreign banks and further provides that all activities of such branches are subject to all consumer laws that apply to their domestic bank competitors. In order to ensure that interstate branching does not allow major banks through their branches to accumulate deposits from communities without making loans, Section 109 requires each appropriate Federal banking agency to promulgate regulations effective June 1, 1997, prohibiting interstate branches from being used as deposit production offices. The regulations must require that if the percentage of loans made by an out-of-state bank in the host state, relative to the deposits taken in the host state, is less than half the average of such percentage for all host state banks, the appropriate federal banking agency shall review its loan portfolio and determine if the out-of-state bank is helping to meet the credit needs of the community it serves. If the agency determines that it is not, it may order the branch to be closed. The provision applies to new interstate branches of national banks, state banks and foreign banks established pursuant to Title I of the bill.

Section 110 of the new law is also aimed at ensuring that banks with interstate branches in several states continue to meet local credit needs in each state in which the

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91. H.R. Conf. Rep. No. 651, 103d Cong., 2d Sess. 53-56 (1994). This report provides an important statement of congressional intent with regard to the power of the Comptroller of the Currency to preempt state law in this area. Also note that the conferees agreed that only the OCC would have the authority to enforce state laws applicable branches of national banks.

bank operates. The Section amends the Community Reinvestment Act (CRA) to provide that an interstate institution receive a separate CRA rating for each state in which it maintains branches.

V. CONCLUSION

The principle provisions of the Riegle-Neal bill governing interstate banking and branching are set forth above. They were carefully crafted to take into consideration the traditional fears in this country about concentrated financial power and to ensure the larger institutions made possible by the bill's passage would continue to serve the credit needs of local communities. They were also drafted to ensure state governments would have a right to opt-out of interstate branching and if they do not opt-out to be able to apply their laws to the out-of-state banks whose branches enter the State. This was to meet concerns expressed by some that interstate branching could weaken the role of state governments in guiding their state's economic development. Meeting such concerns was part of the political process of developing a bill that could get through the Senate and not be opposed by the numerous Senators from smaller states who share the political concerns that have traditionally blocked consideration of interstate banking and branching legislation.

Some commentators believe the new bill will in time strengthen the national bank portion of our dual banking system at the expense of state banks. This is because it will be easier for a bank to branch nationwide with a national bank charter and be subject to just one set of regulators than to have to worry about many state regulators governing its state branches as would an interstate branched state chartered bank. State Bank Supervisors will, no doubt, enter into cooperative arrangements to facilitate state supervision of state banks that branch interstate in order to compensate for the new advantages that the bill gives to a national bank charter as the vehicle for interstate banking.

The authors believe the new law will create a more consolidated banking system as large bank holding companies consolidate their separately chartered banks into branches of the parent bank. In doing so, they will generate substantial savings as they consolidate management, legal services, data processing, compliance and other activities. In addition, the statute permits banks to purchase existing banks and convert them into branches. Although the conversion provision may not be exercised until June 1, 1997—unless a state opts in earlier—banks wishing to position themselves for the enhanced competitive environment will likely be making strategic acquisitions over the next two years.

The authors also expect that over time a few national "champion" banks with international experience will emerge and become partners in assisting U.S. exporters compete more effectively in global markets. This is essential to our country if we are to shed our debtor national status. Such banks with branches throughout the country will be better situated to assist small and medium-sized businesses break into the export market with their international expertise. They will have the knowledge to work with institutions such as the newly created Federal Level Trade Promotion Committee (TPCC). Their overseas branches and agencies working the U.S. embassies and the foreign commercial service will help find export and investment opportunities and help U.S. companies take advantage of them.93

The number of banks in the country will probably shrink from 11,000 less than half that number over the next several years. This will not mean the demise of the community bank, for such banks will continue to play an essential role in local credit markets. It must also be remembered that, even if a community bank is purchased by a larger bank, new banking charters can be secured by those wishing to combine with larger banks in local markets.

In signing the bill, President Clinton expressed the hope that its passage would "mark the beginning of continued efforts to modernize banking laws outdated by technology." This hope reflected the Administration's view that step-by-step reform of our outdated laws governing financial services would stand a better chance of success than the more comprehensive bill sought by the Bush Administration. The Bush Administration proposal attempted to deal with, among other things, interstate banking, Glass-Steagall reform, bank regulatory consolidation, and repeal of the Bank Holding Company Act (the law which separates banking and commerce). Such a proposal created too many opponents as securities firms, small banks, consumer groups, state bank regulators, and others united to kill the legislation. An incremental approach, like that taken with interstate banking, makes the most sense in the present political climate. That is why many experts believe that the resolution of the interstate issue will allow "financial modernization" to be addressed more directly than in past Congresses. It is interesting to note that Congressman Jim Leach [R-IA], the new Chairman of the House Banking Committee, introduced a bill to repeal Glass-Steagall on the first day of the 104th Congress and announced that issue was his top priority. The Chairman of the Senate Banking Committee has also introduced legislation to take on that and other related issues.

On March 1, 1995 Secretary of the Treasury Robert Rubin testified before the House Committee on Banking and Financial Services on Chairman Leach's proposal to repeal Glass-Steagall. The Secretary noted that most major foreign countries permit banks to engage in both commercial and investment banking. Permitting banks to the do the same, he testified, would enhance their competitiveness in the international marketplace and expand the quality of financial services offered at home.

This article has attempted to show that making U.S. banks and the American economy more competitive was a principle consideration behind the formulation and passage of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. That same rationale supports the need to amend the Glass-Steagall Act so that commercial and investment banking functions can be carried out in the same financial institution.

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Section 201 of Title II was enacted to develop a government-wide strategic plan to assist U.S. exporters. U.S. banks should play a major role in assisting the government to implement these provisions.

94. President Bill Clinton Signs Interstate Banking and Branching Efficiency Act of 1994, supra note 2.


