Highlights

Zions Operating Subsidiary Application to Underwrite and Deal in Municipal Revenue Bonds

December 11, 1997

Today the OCC approved an application under Part 5 of its regulations for Zions First National Bank, Salt Lake City, Utah, to underwrite and deal in municipal revenue bonds to a limited extent in an operating subsidiary.

Zions First National Bank was chartered in 1873. It currently has approximately $5 billion in assets, and operates in the states of Utah, Arizona, Nevada, Colorado, California, and Idaho. The bank is well-capitalized, and is the only primary U.S. Government securities dealer operating between Chicago and California.

This is the first OCC approval under its revised Part 5 rule. It will permit a separate subsidiary of a bank to engage in a limited amount of municipal revenue bond underwriting.

Under part 5 a new activity must be part of, or incidental to, the business of banking. This was the case with Zions.

The OCC considered this matter carefully and determined that the law, as well as safety and soundness considerations, clearly favored approval of the bank's proposal. National banks have long-standing experience underwriting and dealing in general obligation bonds and municipal revenue bonds for housing, university, and dormitory purposes, and have demonstrated the ability to perform comparable functions with success.

In addition, national banks may currently invest and trade in municipal revenue bonds, and may hold these securities for years. In underwriting municipal revenue bonds, the subsidiary would generally not hold them for more than a few days. National banks have solid experience in managing any risks associated with these securities.

This approval illustrates the tangible benefits that can flow from financial modernization. It will lower borrowing costs for cities and towns. It will increase the competition for underwriting services, thereby lowering the fees charged municipalities when they issue debt obligations. For some smaller towns, it will enable the jurisdiction to utilize funding options that are not currently available because securities firms have found it not sufficiently profitable to serve the financing needs of some mid-size and smaller communities. In short, more competition means better pricing for municipalities, which translates into lowers costs for cities and municipalities and lower taxes for their taxpayers.

The revenue bond activities of the Zions subsidiary will be subject to full functional regulation by the SEC and the NASD.

The approval does not create safety or soundness problems:

- Under the approval, a national bank must be well capitalized after deducting its investment in the subsidiary from the bank's capital base. This means that even if the subsidiary fails, the national bank will still be well capitalized, the highest capital rating recognized under the banking agencies "prompt corrective action" standards.

- Sections 23A and 23B of the Federal Reserve Act apply to limit bank transactions with the subsidiary. All extensions of credit must be fully collateralized and are limited to a total of 10 percent of the bank's capital.

- The subsidiary must meet all SEC net capital requirements and must have adequate internal controls to manage all risks.

- The bank may not lend to customers to purchase securities during the underwriting, and the bank must make all disclosures required under the Interagency Statement on Nondeposit Investment Products.

The activity the OCC approved for the Zions subsidiary actually is narrower than the municipal revenue bond activity that would have been allowed under H.R. 10, the financial modernization legislation passed by the House Banking Committee. The House Banking Committee version of H.R. 10 would not have limited a bank subsidiary's underwriting and dealing activities to 25 percent of the subsidiary's revenues. In fact, the bill as reported by the Banking

Committee permits bank subsidiaries to underwrite any security without quantitative limitations.

This activity has previously been approved by the Federal Reserve Board for bank holding company subsidiaries. This approval permits a national bank subsidiary to engage in the same activity, and to the same extent, as bank holding company subsidiaries. This approval is consistent with the FDIC's bona fide securities subsidiary rule, under which subsidiaries of state banks are permitted to engage in general securities underwriting and dealing.

The activity is also narrower than the securities underwriting and dealing activity allowed under the Federal Reserve Board's Regulation K for subsidiaries of national banks in foreign markets.