HOLDING CREDIT HOSTAGE FOR UNDERWRITING RANSOM*
RETHINKING BANK ANTITYING RULES

*Christian A. Johnson***

INTRODUCTION

Freed from the shackles of depression age legislation, commercial banks are now in open competition with investment banks for securities underwriting engagements. As commercial banks battle with investment banks over millions of dollars of securities underwriting fees, however, they are attempting to use their lending business as a competitive advantage to secure underwriting mandates. As this high stakes competition heats up, the relatively obscure antitying provisions of the Bank Holding Company Act threaten to influence the outcome, regardless of whether Congress originally intended these rules to do so.

Because underwriting[1] requires less capital and typically generates higher fees than lending, commercial banks are aggressively pursuing opportunities to underwrite debt and equity offerings of public companies, particularly those that are currently customers of the commercial bank. Already, commercial banks are touting their ability to underwrite a customer's securities in addition to their ability to provide bank financing. Securities underwriting, although the most dramatic example, is only one of a number of services that

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* The title was taken from the text of an article by Patrick McGeehan, *Showdown on Wall Street*, N.Y. TIMES, June 15, 2001, at C2 ("they are prohibited from holding credit hostage for underwriting ransom, a practice known in the industry as tying").

 Associate Professor of Law, Loyola University Chicago School of Law. B.A.; MPrA, Utah; J.D., Columbia, 1990. The author gratefully acknowledges the thoughtful and thorough research assistance provided by Heather McDonald and Soula Skokos. The author also acknowledges the helpful comments of Spencer Weber Waller. Loyola University Chicago generously provided research assistance. The views herein are solely those of the author.

1. A securities underwriter acts as a middleman between the company issuing the securities and the public that will purchase the securities. The securities underwriter acts as both an advisor to the company and as a distributor of the securities. Through the securities underwriter, a company issues either debt (such as bonds) or equity securities (such as stock). For a general discussion of securities underwriting, see CHARLES J. JOHNSON, JR., CORPORATE FINANCE AND THE SECURITIES LAWS (1991); HAZEL J. JOHNSON, THE BANKER'S GUIDE TO INVESTMENT BANKING (1996); www.e-analytics.com/ipo (last visited Sept. 22, 2002) which describes the underwriting process; and http:/invest-faq.com/articles/stock-ipo.htm (last revised Nov. 7, 1995).

commercial banks are offering as they wean themselves from their reliance on lending.

Commercial banks offering underwriting will almost always offer these services through a securities affiliate, a company organized by the commercial bank for the purpose of offering underwriting services. These large commercial banks typically operate through a bank holding company structure, with the commercial bank and the securities affiliate operating as affiliates of each other. Commercial banks use securities affiliates to underwrite securities for a variety of historical, practical and operational reasons.[2] For simplicity purposes in this paper, however, it will be assumed that the commercial bank is the actual provider of the underwriting services.[3]

Large money center commercial banks have been particularly interested in underwriting securities, believing this work to be more profitable and less risky than traditional lending. As competition for underwriting engagements increases between commercial banks[4] and investment banks,[5] there has been concern that commercial banks will threaten to withhold bank financing if a customer does not also use the commercial bank as its securities underwriter. Such behavior could constitute a violation of the antitying provisions of the Bank Holding Company Act ("BHCA").[6] Under the BHCA, a commercial bank is prohibited from requiring a customer, as a requirement to extending credit, to purchase additional products or services such as securities underwriting from the commercial bank.

In contrast, investment banks competing with commercial banks for underwriting business are not subject to the BHCA antitying provisions.

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2. *See infra* text accompanying note 68.

3. In addition, traditional antitrust analysis also treats affiliated groups as a single entity.

4. As used in this paper, commercial banks refers to banks whose traditional banking activity has been making loans and collecting deposits. This would normally be financial institutions that are subject to the Bank Holding Company Act, 12 U.S.C. §§ 1841-1850 (2000).

5. Investment banks (or investment bankers) are commonly defined as a "firm, acting as an underwriter or agent, that serves as intermediary between an issuer of securities and the investing public." JOHN DOWNES & JORDAN ELLIOT GOODMAN, BARRON'S FINANCE & INVESTMENT HANDBOOK (1995). Investment banks also typically provide investment advice with respect to mergers and acquisitions, act as broker-dealers for both wholesale and retail clients. The most prominent examples of investment banks includes Merrill Lynch, Goldman Sachs, Bear Stearns and Morgan Stanley among others. Many commercial banks also offer "investment banking" services to their customers but would not necessarily be referred to as an investment bank. *See generally* JOHNSON, *supra* note 1.

6. Bank Holding Company Act Amendments of 1970, Pub. L. No. 91-607, 106(b), 84 Stat. 1760, 1766-67 (codified as amended at 12 U.S.C. § 1972(1) (2000)).

Instead, investment banks are subject to the much looser restrictions on tying found in general antitrust law. Tying is illegal under general antitrust law only if it is anticompetitive in effect with respect to the market for those products and services. In other words, the party must enjoy significant market power for any tying behavior to be illegal. A commercial bank, however, may be liable if the bank's actions were anticompetitive, regardless of the actions' effect on the market. For example, in order to establish liability a plaintiff would only need to show that it was prevented from going to another underwriter, not that the commercial bank dominated the underwriting industry. An investment bank could probably tie the provision of credit to underwriting assignments with relative impunity.

An analysis of the purpose and reach of the antitying provisions in the BHCA is particularly appropriate as commercial banks seek to broaden the services and products that they offer to their customers,[7] such as securities underwriting. As commercial banks expand their underwriting business, it becomes important to understand the extent to which a commercial bank may market both lending and underwriting before it is considered to have tied the services together in violation of the BHCA antitying provisions. Before the repeal of the Glass-Steagall Act, the opportunities to tie the provision of credit to a particular service was quite limited. Now however, banks may try to exploit this competitive advantage through tying.

This analysis is also topical because of the substantial structural changes that are occurring in the commercial banking arena. Already, commercial banks have hired thousands of employees to perform underwriting services on the assumption that they have an unfettered right to underwrite securities and compete with investment banks. These changes are only the beginning as

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7. *See* Matt Ackermann, *Cross-Seller 1st Union Boosts 401(k) Assets*, AMERICAN BANKER, July 7, 2000, at 6 (asset management); *see also* John R. Engen, *E-Brokerage's Integration Challenge*, BANKING STRATEGIES, May-June 2000, *available at* www.bai.org/bankingstrategies/2000-may-june/Articles/E-Brokerage/index.html (banks and e-brokerage); Lynn Striegel, *Training Essential for People Working in Multiple*, AMERICAN BANKER, June 23, 2000, at 16 ("extensive menu of products and services such as insurance, broker-dealers services, mortgages, mutual funds, investment advice, and new finance-related business"). Some view these goals as unrealistic however. Steve Klinkerman, *The Specialist Challenge*, BANKING STRATEGIES, Mar.-Apr. 2000, at 42 (interviewing Clayton Christensen, Harvard Business Professor—"It's a pipe dream to think that financial services conglomerates can simultaneously maintain the state of the art in online banking, and equities underwriting, and wealth management, and insurance, and so on."), *available at* www.bai.org/bankingstrategies/2000-Mar-Apr/Articles/specialist_challenge/index.html.

commercial banks transform themselves by offering additional services such as insurance, merger and acquisition advice, and derivative products, among others.

Banks, regulators and Congress need to address the role of the antitying rules in this new regulatory environment. In freeing commercial banks from the shackles of Glass-Steagall, Congress was determined to permit commercial banks to compete on an even footing with investment banks, in particular with respect to underwriting. Inadvertently, however, Congress has drastically increased the possibility of commercial banks engaging in anticompetitive behavior. Commercial banks in their efforts to compete with investment banks may exploit these newly found banking powers through tying new services to their lending business.

Application of the antitying rules to this new world, however, also presents risks. Aggressive application of the BHCA antitying provisions could wreak havoc on tens of millions of dollars of investments in the underwriting arena made by commercial banks. In addition, the sheer extent of potential damages has changed as commercial banks move into underwriting. As commercial banks earn hundreds of millions of dollars in underwriting fees, damages stemming from application of these antitying rules could be equally as high, dwarfing any prior award of damages under the statute.

There have been numerous cases litigated over the past several decades involving the BHCA antitying provisions. However, the majority of these cases do not deal with the sophisticated and complex types of activities that many commercial banks are currently engaged in such as securities underwriting. In addition, the case law and statutory provisions were not decided or passed in this new competitive environment. Although commentators worry about banks tying the provision of credit to other products or services,[8] few appear to have focused on the issue of tying credit to securities underwriting.[9]

There is no statutory, regulatory or case law under the BHCA that resolves or even discusses how the antitying provisions should be applied to the tying of lending and underwriting. Even more problematic is that the enactment of the BHCA antitying provisions pre-date the repeal of the Glass-Steagall provisions that prohibited a commercial bank (or a securities affiliate) from underwriting securities. On at least a superficial level, under existing law it appears that commercial banks are on the verge of violating the statute. Congress and the courts should consider the role the antitying provisions should take as commercial banks and investment banks battle in the underwriting arena.

Part I of this article will discuss the history of commercial banks' powers to both lend and underwrite securities, focusing particularly on the enactment of the Glass-Steagall restrictions and their repeal by the Gramm-Leach-Bliley Act of 1999. It will also focus on the recent rise of commercial banks (or their affiliates) as securities underwriters. In viewing this history, it is important to appreciate how drastically the capital markets landscape has changed over the past decade.

Part II will examine the growing convergence of commercial banks and investment banks both offering credit and underwriting services. This convergence appears to be driven by the customer's demand for credit, whether it is provided by a commercial bank or an investment bank. Large customers are often requiring securities underwriters to act also as a lender if they want the customer's underwriting business, commonly referred to as "pay to play."

Commercial banks, prepared to lend as well as underwrite, have attempted to step into the void as investment banks have balked at committing

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8. Commentators have become concerned about possible ties between the provision of credit and over-the-counter derivatives. *See* Barry Taylor-Brill, *Negotiating and Opining on ISDA Masters*, 1147 PLI/Corp 79, 92 (1999) ("[A]ny U.S. bank(s) which impose the following types of restrictions and requirements should consider their liability under [the antitying rules of the BHCA]"); L. Clifford Craig et al., *Legal Theories in Lawsuits Against Derivatives Dealers in the Over-the-Counter Markets*, 931 PLI/Corp 129, 168-69 (1996) ("[T]he facts of a particular case may indicate that such a cause of action is viable").

9. *See*, *e.g.*, Patrick McGeehan, *Showdown on Wall Street*, N.Y. TIMES, June 15, 2001, at C1. McGeehan notes that "Banks have to tiptoe around the issue because they are prohibited by regulators from holding credit hostage for underwriting ransom, a practice known in the industry as tying."

capital to lending activities. Commercial banks are offering customers inexpensive loans in order to land lucrative securities underwriting mandates. As commercial banks use this competitive advantage, investment banks are crying foul based on potential violations of the BHCA antitying provisions.

Finally, Part III discusses the elements of a tying claim under the BHCA in light of the dramatic restructuring of U.S. capital markets brought upon by the repeal of Glass-Steagall. Part III then analyzes whether, once the elements have been satisfied, such a tying claim can be sustained under the BHCA. Application of these antitying provisions is important in view of commercial banks' aggressive entry into the securities underwriting market. Failure to apply and enforce these rules could result in an unfair and anticompetitive advantage for the commercial banks. Part III argues that Congress did not intend for commercial banks to capitalize on such a competitive advantage through anticompetitive tying activities. Courts, banking regulators and the Department of Justice need to take an active part in policing commercial banks anticompetitive activities and enforcing the antitying provisions if such behavior is going to be controlled.

I. Power to Underwrite Securities

The law governing the underwriting of securities by commercial banks has come full circle in the past 70 years. Although the current competition over the offering of underwriting services between commercial and investment banks is relatively new, it mirrors much of the competition that took place in the 1920s and 1930s. For reasons unrelated to antitying concerns, Congress took away the power of commercial banks to underwrite securities in the 1930s and has only recently restored them. Taking advantage of new statutory powers, commercial banks are competing aggressively with investment banks over underwriting engagements.

A. Glass-Steagall Restrictions Against Underwriting Securities

The Glass-Steagall Act,[10] also known as the Banking Act of 1933, was enacted to separate the commercial banking world from the investment banking world.[11] Prior to the enactment of the Act, many commercial banks were engaged in investment banking activities either directly or indirectly through securities affiliates.[12] The Glass-Steagall Act not only prohibited banks from engaging in investment banking activities directly, but also prohibited banks from being affiliated with organizations that were engaged in such activities.[13]

Commercial banks and nationally chartered banks appear to have entered the world of investment banking as a response to competition posed by a new phenomenon to the banking world: trust companies.[14] At the time, trust companies were very attractive to customers because they were able to offer a wide variety of services including corporate security issues.[15] In response to the increase in competition, state banks began to demand similar competitive powers from their legislatures.[16] State legislatures generally met the banks' demands and the difference between the underwriting powers of

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10. 12 U.S.C. §§ 21, 22-24, 25a-29, 35-37, 39, 51-53, 55-57, 59-62, 66, 71, 72-76, 81, 83-91, 93, 94, 101a, 102, 104, 107-110, 123, 124, 131-138, 141-144, 151, 152, 161, 164, 168-175, 181-186, 192-196, 481-485, 501, 541, 548, and 582 (2000).

11. MELANIE L. FEIN, SECURITIES ACTIVITIES OF BANKS § 4.01 (3d ed. 1997).

12. Inv. Co. Inst. v. Camp, 401 U.S. 617, 629 (1971). By 1922, sixty-two commercial banks were directly engaged in investment banking while ten others had formed securities affiliates. Edwin J. Perkins, *The Divorce of Commercial and Investment Banking: A History*, 88 BANKING L.J. 483, 492 (1971).

13. *Camp*, 401 U.S. at 629.

14. Perkins, *supra* note 12, at 486-89. During the post-Civil War era, trust companies sprang up as a new type of financial institution. At first, trust companies were specialized in the areas of estate and will administration but eventually expanded into traditional commercial banking activities such as soliciting deposits from the public. Many customers found trust companies to be very attractive because of the large range of services that they offered that were not found in commercial banks. Additionally, trust companies also "became involved in the preparation and distribution of corporate security issues." Consequently, trust companies became very familiar with the interrelationships of the financial markets. This gave trust companies an even greater competitive advantage over commercial banks by being able to offer customers a more well rounded and balanced advice from their knowledge of the financial markets. In addition, by offering various types of services to their customers in one institution, trust companies were able to offer a "department store" style of banking to its customers. *Id.* at 486-88.

15. *Id.* at 487.

16. *Id.* at 488.

state banks and trust companies eventually became minimal.[17] State banks, however, had fewer restrictions than banks chartered under the National Banking Act.[18] In an effort to stay competitive, many nationally chartered banks made plans to enter the investment banking field by using their incidental corporate powers to conduct banking business.[19] Eventually, a large number of securities affiliates sprang up as subsidiaries of national banks.[20]

The securities affiliates of national banks became formally recognized by Congress with the passage of the McFadden Act in 1927.[21] With this enactment, Congress chose to recognize the investment securities business of banks as an existing bank service instead of granting a new power.[22] The Act amended the law relating to the corporate powers of national banks by adding the following statement to the statute:

> That the business of buying and selling investment securities shall hereafter be limited to buying and selling without marketable recourse obligations . . . commonly known as investment securities, under such further definition of the term "investment securities" as may by regulation be proscribed by the Comptroller of the Currency . . . .[23]

The Comptroller of the Currency, therefore, was given the duty of determining what types of securities were eligible for affiliates to underwrite.[24]

The recognition of the securities affiliates under the McFadden Act combined with the rise in stock market prices from 1927 to 1929, resulted in commercial banks becoming increasingly active in the securities markets.[25] By 1930, however, the existence of the affiliate system was threatened. The failure of the Bank of the United States in December 1930 was largely

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17. *Id.* at 488-89.

18. *Id.* at 489. For a discussion of state versus national bank banking powers, see Christian Johnson, *Wild Card Statutes, Parity and National Banks—The Renascence of State Banking Powers*, 26 LOY. U. CHI. L.J. 351 (1995).

19. Gerald T. Dunne, *Glass-Steagall Act—A History of Its Legislative Origins and Regulatory Construction*, 92 BANKING L.J. 38, 39 (1975). The First National Bank of New York had already entered the investment banking market by creating one of the first securities affiliates of a nationally chartered bank. Perkins, *supra* note 12, at 489.

20. Perkins, *supra* note 12, at 489.

21. *Id.* at 494.

22. Dunne, *supra* note 19, at 39.

23. McFadden Act, Section 2(b), 44 Stat. 1226, codified at 12 U.S.C. § 24. For a discussion of the change, see Dunne, *supra* note 19, at 39-40.

24. Perkins, *supra* note 12, at 494.

25. *See id.* at 495.

attributed to its activities with respect to its securities affiliates.[26] Consequently, the Bank's failure raised suspicion among many politicians and the general public of the securities activities of all commercial banks.[27]

The Glass-Steagall Act reflected Congress' concern that commercial banks in general had been damaged by the stock market decline partly because of their direct and indirect involvement in the trading and ownership of speculative securities.[28] The Act acknowledged that potential hazards and financial dangers existed in allowing commercial banks to enter the world of investment banking.[29] Congress was not only concerned that a commercial bank would invest its own assets in imprudent stock or securities investments, but also that a commercial bank would give unsound aid or loans to its securities affiliate to maintain public confidence in that institution.[30]

Congress feared that in an effort to make the securities affiliate successful, commercial banks would make their credit facilities more freely available to companies in whom their securities affiliates had invested.[31] Congress also worried that commercial banks might even go to the extent of making unsound loans to such companies.[32] In essence, Congress believed that commercial banks were not capable of promoting their investment banking activities without undermining its role as a disinterested source of credit.

Another perceived hazard was that commercial bank depositors might have incurred losses on investments that they had purchased from affiliates because of their reliance on the bank's relationship with the affiliate.[33] Congress believed that a commercial bank could not lend that reputation of "prudence and restraint" to a securities affiliate and not have its reputation

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26. *Hearings Pursuant to S. Res. 71 before a Subcomm. of the Senate Comm. on Banking & Currency*, 71st Cong., 3d Sess., 116-117, 1017, 1068 (1931) [hereinafter *1931 Hearings*].

27. Perkins, *supra* note 12, at 497.

28. S. REP. NO. 77, 73rd Cong., 1st Sess., 6, 8, 10.

29. *1931 Hearings*, *supra* note 26, at 365.

30. *Id.* at 20, 237, 1063.

31. Inv. Co. Inst. v. Camp, 401 U.S. 617, 631 (1971).

32. *1931 Hearings*, *supra* note 26, at 1024.

33. *See* 77 CONG. REC. 4023, 4028 (1933). Congress was afraid that banks were advising depositors to take their money out of the banks and invest in bonds that depositors knew nothing about. *Id.* Congress feared that depositors simply relied on the banks' reassurances of: "Of course our bank is behind them, and that is enough, for we have investigated them." *Id.*

undercut by the ultimate risks involved in investment banking.[34] Additionally, Congress was concerned that commercial banks might be tempted to make loans to its customers with the expectation that the loan would assist the customers in buying securities from the affiliates.[35]

Congress essentially believed that investment banking activities were detrimental both to public confidence in the commercial banking system, and a commercial bank's ability to be prudent and restrained.

B. The Erosion and Repeal of Glass-Steagall Restrictions

Although the Glass-Steagall Act was adopted in 1933 in an effort to separate the commercial banking world from the investment banking world, the line dividing the two worlds became moderately relaxed in the years that followed. By the early 1950's, in response to the competition posed by the revived investment banking industry, commercial banks began to search for loopholes around the prohibitions of the Glass-Steagall Act.[36] One such loophole was found when commercial banks formed bank holding companies, essentially corporate shells, to conduct both banking and non-banking practices.[37] Congress responded by enacting the Bank Holding Company Act (BHCA) of 1956[38] to close the loophole left by the Glass-Steagall Act.

The BHCA in essence prohibited bank holding companies from conducting non-banking activities and gave the Federal Reserve the authority to allow bank holding companies to engage in activities it determined to be "closely related to banking or managing or controlling banks as to be a proper incident to."[39] As the Federal Reserve, however, began to liberalize its policies concerning the ability of banks and bank holding companies to acquire and control non-bank subsidiaries, the line that was clearly drawn by the Glass-Steagall Act between commercial and investment banking began to blur.[40]

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34. *See* 75 CONG. REC. 9908, 9912.
35. S. REP. NO. 77, 73rd Cong., 1st Sess., 9-10.
36. Jonathan Zubrow Cohen, *Comment: The Mellon Bank Order: An Unjustifiable Expansion of Banking Powers*, 8 ADMIN. L.J. AM. U. 335, 344 (1994).
37. *Id.* at 344-45.
38. The Bank Holding Company Act of 1956, codified at 12 U.S.C. §§ 1841-50 (2000).
39. 12 U.S.C. § 1843(c)(8).
40. *See* Cohen, *supra* note 36, at 340.

The Supreme Court also played a role in blurring the line between the commercial and investment banking world by endorsing a "policy of deference to statutorily authorized administrative agencies."[41] In *Investment Co. Institute v. Camp*, the Court recognized that, "courts should give great weight to any reasonable construction of a regulatory statute adopted by the agency charged with the enforcement of that statute."[42] In *Camp*, the Court concluded, however, that it could not simply defer to the Comptroller of Currency because the Comptroller failed to articulate the "meaning and impact" of Sections 16 and 21 of the Glass-Steagall Act on collective investment funds when it promulgated Regulation 9 which permitted banks to operate collective investment funds.[43] After an extensive analysis of the legislative intent of the Glass-Steagall Act, the Court held that the Comptroller's Regulation 9 violated Sections 16 and 21 of the Glass-Steagall Act.[44]

Although the Court did not defer to the Comptroller of the Currency in *Camp*, the Court did indicate that it would defer to any reasonable interpretation of the Act.[45] Thus, banking regulators would be free to permit new non-banking activities without judicial interference as long as regulators were able to set forth a reasonable interpretation of the Act.[46] Therefore, in *Federal Reserve System v. Investment Co. Institute*, the Court upheld the Federal Reserve's amendments to Regulation Y which permitted banks to act as investment advisors to closed-end companies.[47] The Court, in reiterating the deference it recognized in *Camp*, agreed with the Board's interpretation of the difference between an open investment fund and a closed investment fund and concluded that the amendments did not violate the Glass-Steagall Act.[48]

By the early 1980s, the Comptroller of the Currency, the Board of Governors of the Federal Reserve, and the courts each began to play a role in

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41. *Id.* at 349. The key Supreme Court decisions that indicate a general trend towards a policy of judicial deference include: *Inv. Co. Ins. v. Camp*, 401 U.S. 617 (1971); *Fed. Reserve Sys. v. Inv. Co. Inst.*, 450 U.S. 46 (1981); *Securities Industry Ass'n v. Fed. Reserve Sys.*, 468 U.S. 207 (1984).

42. *Camp*, 410 U.S. at 626-27.

43. *Id.* at 627.

44. *Id.* at 639.

45. Cohen, *supra* note 36, at 352.

46. *Id.*

47. Fed. Reserve Sys. v. Inv. Co. Inst., 450 U.S. 46 (1981).

48. *Id.* at 51.

reinterpreting the restrictions of the Act[49] which in effect blurred the clear line that the Glass-Steagall Act once drew between commercial and investment banking.

By the 1990s, many felt that the economic boom required an increase of the efficiency and competition in the financial markets and that those goals could be facilitated by a reform or repeal . . . repeal of the Glass-Steagall Act.[50] In response to the call for reform, Congress introduced the Gramm-Leach-Bliley Act ("GLB Act"), which was signed into law on November 12, 1999 and provided for a major overhaul of the Glass-Steagall Act.[51] Although the Glass-Steagall Act was not repealed in its entirety, significant portions of it were repealed.

In particular, Section 20 was repealed which prohibited member banks of the Federal Reserve system from affiliating with any company that "engaged principally in the issue, floatation, underwriting, public sale or distribution" of securities.[52] Additionally, the GLB Act repealed Section 32 of the Glass-Steagall Act, which prohibited any officer, director, employee or partner of a securities firm from ever serving "at the same time as an officer, director, or employee of any member bank . . . ."[53] Thus, the GLB Act removed all of

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49. *Id.*

50. *See*, *e.g.*, Robert W. Dixon, *The Gramm-Leach-Bliley Financial Modernization Act: Why Reform in the Financial Services Industry was Necessary and the Act's Projected Effects on Community Banking*, 49 DRAKE L. REV. 671, 679 (2001). Alan Greenspan, Chairman of the Federal Reserve Board, strongly lobbied for the repeal of the Glass-Steagall Act and noted:

> In the United States, our financial institutions have been required to take elaborate steps to develop and deliver new financial products and services in a manner that is consistent with our outdated laws. The costs of these efforts are becoming increasingly burdensome and serve no useful purpose. Unless soon repealed, the archaic statutory barriers to efficiency could undermine the global dominance of American finance . . . .

Financial Services Modernization Act of 1999: Hearings on H.R. 10 before the Comm. on Banking and Financial Servs. of the U.S. House of Representatives, 106 Cong. 254 (1999) (Statement of Alan Greenspan, Chairman, Federal Reserve Board of Governors).

51. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338 (1999). For a general discussion of the Gramm-Leach-Bliley Act, see Dixon, *supra* note 50, at 672; Paul J. Polking & Scott A. Cammarn, *An Overview of the Gramm-Leach-Bliley Act*, 4 N.C. BANKING INST. 1 (2000); Joseph A. Smith, Jr., *Retail Delivery of Financial Services After the Gramm-Leach-Bliley Act: How Will Public Policy Shape the "Financial Services Supermarket"?*, 4 N.C. BANKING INST. 39 (2000); Karol K. Sparks, *Freeing the Banks*, BUS. L. TODAY, Aug. 10, 2001, at 10.

52. 12 U.S.C. § 377.

53. 12 U.S.C. § 78.

the restrictions the Glass-Steagall Act placed on the affiliations between commercial banks and investment banks.[54]

In further relaxing the separation between commercial banking and investment banking, the GLB Act allowed for the creation of "financial holding companies" (FHCs) which permitted the affiliation of securities firms, depository institutions, insurance firms and other financial institutions.[55] An FHC is a bank holding company that may engage in any activity that is determined by the Federal Reserve Board to be: "i) Financial in nature or incidental to such financial activity or ii) complementary to a financial activity and does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally."[56]

The Act expressly states that the following list of activities are deemed to be financial in nature:

- Underwriting, dealing and making a market in securities[57]
- Merchant banking or venture capital[58]
- Mutual fund activities (advisor, distributor, administrator, seller, sponsor)[59]
- Lending, exchanging, transferring, investing for others, or safeguarding money or securities[60]

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54. Securities Law Handbook § 1.07 (Harold S. Bloomenthal ed., 2001).

55. *Id.* The Gramm-Leach-Bliley Act, however, places conditions on banks and their financial subsidiaries:

- The bank's investment in, and retained earnings of, the financial subsidiary must be deducted from the capital of the bank, 12 U.S.C. § 24a(c)(1)(A);
- The assets and liabilities of the financial subsidiaries may not be consolidated with the parent bank, § 24a(c)(1)(B);
- The bank must establish procedures for managing financial and operational risks associated with the bank and the financial subsidiary, § 24a(d)(1);
- The bank must insure that the financial subsidiary has a separate corporate identity, § 24a(d)(2);
- The assets of the financial subsidiary, when combined with the assets of all other financial subsidiaries owned by the bank, can not exceed 45% of the parent bank's assets or $50 billion, whichever is less, § 24a(2)(D);
- The affiliate restrictions of § 23A and B of the Federal Reserve Act apply, except that the 10% of capital limitation as to extensions of credit or investments in any one subsidiary are not applicable. Instead, no more than 20% of the bank's capital may be lent to or invested in all financial subsidiaries. § 371c(c)(3)(A).

56. 12 U.S.C. § 1843(k)(1).

57. Section 1843(k)(4)(E).

58. Section 1843(k)(4)(H).

59. Section 1843(k)(4)(G).

60. Section 1843(k)(4)(A).

- Issuing or selling asset-backed securities[61]
- Engaging in any activity the Board has determined, by order or regulation that is in effect on the date of the enactment of the GLB Act, to be so closely related to banking or managing or controlling banks as to be a proper incident thereof.[62]

Through these new financial vehicles, investment banks, commercial banks, and insurance companies are permitted to come together to provide virtually all types of financial services to consumers previously expressly prohibited under the Glass-Steagall Act.

The GLB Act, however, did not significantly alter the sections of the Glass-Steagall Act addressing the activities that commercial banks may engage in directly. The section of the Glass-Steagall Act that governs the direct securities activities of commercial banks, Section 16, was not repealed.[63] Section 16 was amended by the GLB Act to expand commercial banks' authority to underwrite by authorizing national banks that are well capitalized to underwrite, deal or purchase in municipal revenue bonds.[64] However, with respect to underwriting, Section 16 provides that with certain exceptions, a national bank is prohibited from underwriting "any issue of securities or stock."[65] The restrictions under Section 16, thus, do not apply to underwriting securities that are "obligations of the United States, or general obligations of any State or of any political subdivision thereof . . . ."[66] Therefore, national and state member banks are authorized to underwrite U.S. government securities and general obligation bonds of U.S. state and local governments.[67]

C. *Commercial Banks as Securities Underwriters*

Although restrictions on commercial banks against underwriting securities have only recently been completely lifted, already some of the most active securities underwriters are commercial banks. As commercial banks

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61. Section 1843(k)(4)(D).
62. Section 1843(k)(4)(F).
63. Section 24.
64. GLB Act § 151, *amending* § 16 of the Glass Steagall Act, 12 U.S.C. § 24.
65. 12 U.S.C. § 24.
66. *Id.*
67. *Id.*

have become more sophisticated in the area, it has become easier for them to compete with traditional investment banks.[68]

Currently, the vast majority of large commercial banks in the United States underwrite securities, either directly or through an affiliate.[69] For example, JP Morgan Chase hopes to marry its lending and its underwriting business together in its efforts to further develop its investment banking activities.[70] Commercial banks hope that combining lending with underwriting will give them an edge over investment banks.[71]

Commercial banks offer a full range of securities underwriting services for their customers. Both Bank of America and Bank One tout their abilities to underwrite all types of securities.[72] Chase Manhattan Bank notes that it "is an underwriter and market-maker in corporate debt securities, including medium term notes, private placements and 144A issues; asset-backed securities, mortgage-backed securities, federal agency securities and money market securities, including commercial paper."[73] Finally, Citibank "ranks at

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68. Adam Tempkin, *Muscling In: Commercial Banks Take Over ABS*, INVESTMENT DEALERS DIGEST, July 30, 2001 ("'But now that distribution and cost of distribution is not such a big issue, the firms associated with credit providers are much more competitive . . . .'" quoting Alex Roever), *available at* 2001 WL 7994692.

69. The following banks had significant securities underwriting businesses: Bank of America Corporate & Institutional Banking, //corp.bankofamerica.com, Sept. 12, 2001 (capital markets page); Bank One, www.bankone.com (Capital markets products—high yield securities & Investment Grade Securities pages); York; Bank One, NA; Chase Manhattan Bank, www.chase.com (High grade corporate securities page), Sept. 12, 2001.; Citigroup, www.citigroup.com (Global corporate business page), Sept. 12, 2001; First Union National Bank, //business.firstuion.com (investment grade debt page), Sept. 12, 2001; Fleet Bank, www.fleet.com (Capital raising page), Sept. 12, 2001; Boston Financial Corporation; Keybank, www.keybank.com (Investment banking page), Sept. 12, 2001; Mellon Bank, www.mellon.com (Mellon corporate financing page), Sept. 12, 2001; PNC Bank, www.pncbusinesscredit.com ((products and services page), Sept. 12, 2001; State Street Bank & Trust Company, www.statestreet.com (Investment banking page), Sept. 12, 2001; Suntrust Bank, www.suntrust.com, (Investment banking page), Sept. 12, 2001; Wells Fargo Bank.

70. Gary Silverman, *JP Morgan Chase Issues Gloomy Report*, FINANCIAL TIMES, June 7, 2001, at 32.

71. *Id.*

72. Bank of America, through its underwriting affiliate Bank of America Securities, "provides full-service underwriting capabilities, including origination, sales, trading and research, for public and 144A high yield debt securities." Bank of America Corporate & Institutional Banking, http://corp.bankofamerica.com (last visited Sept. 12, 2001). Bank One "originates, underwrites, trades, distributes and provides research on investment grade securities and high yield securities," underwriting over $12 billion in high yield securities since 1996. www.Bankone.com (last visited Sept. 12, 2001).

73. www.chase.com (High grade corporate securities page) (last visited Sept. 12, 2001).

or near the top by most important industry measures in its principal investment banking activities: global and U.S. underwriting of equity and debt."[74]

Not only are commercial banks underwriting securities, but they are quickly competing with the major investment banks that have traditionally dominated the area.[75] Frequently U.S. commercial banks go head to head with investment banks over underwriting assignments in the United States.[76] Additionally, similar trends have also been noted in Europe as foreign commercial banks move toward fee and commission business.[77]

In the year 2000, U.S. commercial banks appeared to be competing on an almost equal basis with traditional Wall Street investment banks. In a survey by Investment Dealers Digest, Salomon Smith Barney (an affiliate of Citibank), JP Morgan Chase (an affiliate of Chase Manhattan Bank), BofA Securities (an affiliate of Bank of America), and First Union Securities (an affiliate of First Union National Bank) were all among the top 15 underwriters of U.S. debt and equity offerings in the United States.[78] In addition to those four, several other banks were also listed in the top 15 of several of the more specialized underwriting categories.[79]

Commercial banks believe that securities underwriting will prove to be an important part of their profitability in the future. Equity underwriting, for example, commands some of the highest fees on Wall Street.[80] Further, underwriting is considered to be "low risk and immensely profitable."[81] Conversely, commercial bank lending carries "big risks but generates minimal returns."[82]

For example, during the first five months of 2001, Citibank, through its securities affiliate, earned over $985 million in fees from its debt and equity

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74. www.citigroup.com (Global corporate business page) (last visited Sept. 12, 2001).

75. For a discussion of investment banking activities of banks, see HAZEL J. JOHNSON, THE BANKER'S GUIDE TO INVESTMENT BANKING 149-166 (1966).

76. *See* McGeehan, *supra* note 9, at C11 (giving examples of Citibank and Chase competing for underwriting business).

77. *Investment Banking*, THE BANKER, Oct. 1, 2000.

78. *Domestic Rankings*, INVESTMENT DEALER'S DIG., Jan. 8, 2001, at 43.

79. *Id.* at 43-59 (First Tennessee Bank, Wells Fargo Bank, Bank One, US Bankcorp, FleetBoston Financial (an affiliate of Fleet Bank)).

80. Suzanne McGee, *Deal & Deal Makers Chase Uses Its Lending Clout to Land Underwriting Work*, WALL ST. J., Dec. 23, 1999, at C20; *see also* JOHNSON, *supra* note 1, at 40-41 (discussing compensation).

81. Derek DeCloet, *Massive Profit, Minimal Risk*, NAT'L POST, July 18, 2001, at C3.

82. *Id.*

underwriting.[83] The Chase Manhattan Bank, through its securities affiliate earned $336 million during the same period.[84] Bank of America was similarly successful, earning $248 million in equity and debt underwriting fees during the same period.[85] Individual transactions can be equally lucrative.[86] In an initial public stock offering, for example, "the underwriter's discount or commission usually ranges from 7 percent to 9 percent of the public offering price of a new common stock issue."[87]

II. The Growing Convergence of Lending and Underwriting

As commercial banks have become increasingly active in the securities underwriting market, two trends have emerged with respect to lending and underwriting. First, large Fortune 500 companies, as they scramble to secure and maintain credit lines, are beginning to require that their securities underwriters also act as lenders, regardless of whether they are a commercial bank. Many investment banks are finding that even long term clients are threatening to cut them off from underwriting engagements if the investment bank is not also willing to lend to them.

Second, commercial banks are using their lending business as a competitive advantage over investment banks. Commercial banks are using their ability to make low-cost bank loans to entice companies to use them as underwriters. Companies have been willing to use commercial banks as securities underwriters in order to take advantage of the credit that a commercial bank will extend to it. From an antitrust perspective, both investment banks and customers are concerned that commercial banks will attempt to leverage their competitive lending position by explicitly or implicitly requiring a borrower to use them as its securities underwriter.

What appears to unite this convergence is the increasing difficulty of obtaining credit. A tighter credit market appears to be changing the behavior of commercial banks, investment banks, and customers. Large public corporations are using their market muscle to increase or at least maintain the

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83. McGeehan, *supra* note 9, at C2.
84. *Id.*
85. *Id.*
86. McGeehan, *supra* note 9 (explaining Chase earned more than $3 million managing a bond sale for Venator Group).
87. www.granthornton.com (Costs of going public page) (last visited Oct. 4, 2001).

amount of credit available to them. Smaller and more vulnerable institutions are discovering that they are giving securities underwriting mandates to their commercial banks in order to maintain important bank credit lines. Although the convergence is only beginning, it is important to assess the impact of the BHCA antitying provisions on commercial banks participation.

A. Tightening Credit Markets

The lending and credit markets are tightening in the United States. The tightening appears to have several causes. First, as the economy weakens, commercial banks have become more cautious in their lending activities, demanding better terms and lending less. Second, the continuing consolidation of the banking industry also appears to be limiting the amount of credit available.

1. Economic Conditions

As the economy slows,[88] commercial banks have become increasingly concerned about loan defaults, with many borrowers struggling to repay loans.[89] A variety of problems such as "ratings downgrades, declining revenues, and outright defaults" continue to discourage lenders from greatly increasing bank credit.[90] Commercial banks are already beginning to slow

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88. Customers are becoming more concerned about credit availability after September 11th. *See* Jathon Sapsford et al., *Attacks Derailed Keefe-BNP Talks*, WALL ST. J., Oct. 10, 2001, at C1; *see also* Jathon Sapsford & Paul Sherer, *Deal & Deal Makers: Fewer Banks Mean Costlier Credit Lines*, WALL ST. J., Mar. 14, 2001, at C1 ("A slowing economy and rising defaults are major factors.").

89. Rich Miller & Heather Timmons, *A New Credit Crunch*, BUS. WK., Feb. 18, 2002, at 32-33 ("Bad loans at big commercial banks have jumped nearly 30%"). For example, Bank of America, as well as Citibank and Chase, continue to struggle because of loan losses. Jathon Sapsford, *Bank of America Profit Falls 54%, as Loan Losses Show Challenges*, WALL ST. J., Oct. 16, 2001, at C1.

90. Phyllis Berman, *Forbes Global*, www.forbes.com/global/2000/1225/032602/a.html (last visited Dec. 25, 2000) ("Bank examiners have been swarming over syndicated-loan portfolios at several leading banks and forcing downgrades."); Mitchell Pacelle, *Waiving or Drowning: Banks Face Loan Bind*, WALL ST. J., Oct. 15, 2001, at C1 ("federal regulators . . . reported a rise in syndicated bank loans that are likely to default."); Joseph Segar, *Syndicated Loans Post 6% Gain*, INVESTMENT DEALERS DIG., July 16, 2001; Julie Watson, *Bank Earnings Firm, Despite Credit Concerns*, www.forbes.com/2001/04/19/0419earnings2.html (last visited Apr. 19, 2001) ("Pressure on both retail and commercial [loan] portfolios.").

down the lending that they are doing[91] in all market segments.[92] As credit becomes more difficult to obtain, bank credit lines will become increasingly more important for borrowers.[93]

In response, commercial banks have begun to tighten their lending standards, making it increasingly difficult for borrowers to find the bank financing that they need.[94] Even when bank loans are available, borrowers discover that these loans are more expensive,[95] limiting the amount they can afford to borrow.[96] Not only are bank loans becoming more expensive because of higher interest rates, but commercial banks are also "tightening loan covenants, beefing up collateral requirements."[97]

2. *Banking Consolidation*

Over the past decade, the banking industry has rapidly consolidated. Even the largest commercial banks find themselves being sold and purchased. Unfortunately, one of the net effects of this consolidation, however, has been the reduction of the amount of bank credit available in the market, especially for larger credits. Consolidation is lessening competition not only for large customers, but also in the middle market.[98]

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91. *Less Credit Where Credit is Due*, BUS. WK., July 22, 2002, at 68, 69; *Big Banks, Little Lending*, BUS. WK., May 12, 2002, at 54; Miller & Timmons, *supra* note 89, at 32-33 (banks "will opt to lend less"); Anna Schiffrin, *Underwriters Under a Cloud*, INDUSTRY STANDARD, Dec. 11, 2000, at 86.

92. Sapsford, *supra* note 89.

93. Miller & Timmons, *supra* note 89, at 32 ("in some cases, forcing companies to turn to banks for even more costly cash"); *The Great League Table Debate*, EUROMONEY, June 2001, at 116; Gregory Zuckerman, *Despite Rebound, Fears of Corporate Credit Crunch Linger*, WALL ST. J., July 25, 2002, at C1; Robert Lenzner & Matthew Swibel, *Warning: Credit Crunch*, FORBES, Aug. 12, 2002, at 62.

94. Robert S. England, *Loans Anyone?*, BANKING STRATEGIES, May/June 2001, at 54; Miller & Timmons, *supra* note 89, at 32 (explaining that banks are "tightening lending terms and cutting off companies that don't pass muster."); Mitchell Pacelle, *Waiving or Drowning*, WALL ST. J., Oct. 15, 2001, at C1 (discussing tightening standards).

95. Miller & Timmons, *supra* note 89, at 32 (credit is getting "costlier"); Sapsford & Sherer, *supra* note 88, at C1 ("Companies will probably end up paying more for credit lines.").

96. England, *supra* note 94, at 54 ("Many firms are being asked to pay widening spreads for loans and limit their total debt."); Sapsford & Sherer, *supra* note 88, at C1 ("Companies are already scaling back credit lines, either because of higher pricing or because money just isn't available.").

97. England, *supra* note 94, at 56.

98. Hung Tran, *Lending Continues to Give GPs Headaches, Buyouts*, Sept. 2, 2000, *available at* 2001 WL 7994494.

As a result of consolidation, there are fewer lenders in the banking industry. Approximately 500 commercial banks and savings institutions were "absorbed by mergers in 2000."[99] Recently, large commercial bank mergers have made history such as the mergers of Bank of America and Nationsbank,[100] and the merger of First Union National Bank and Wachovia Bank.[101]

Syndicated lending has been hit particularly hard because of consolidation.[102] Syndicated bank loans are transactions in which several commercial banks will join together to make one large loan to a particular borrower.[103] The number of commercial banks participating in syndicated bank loans have declined from "110 lenders to 49 lenders in the past three years," principally because of consolidation.[104] Although the loan is typically managed by one commercial bank acting as an administrative agent for the others, each commercial bank may lend tens of millions of dollars as a member of the banking group. Syndicated loans are particularly important because large public customers will often borrow hundreds of millions of dollars at a time.

As consolidation occurs, borrowers have discovered that the amount of credit available will be reduced by the combined financial institutions.[105] In particular, when commercial banks combine, they typically do not make available the same total amount of credit as was made available by the individual institutions prior to consolidation.[106] Lenders have noted that over time, the syndicated loan market is not improving.[107] Commercial banks are less willing to enter into syndicated lending because syndicated loans are often viewed as unprofitable. Lenders currently view most syndicated loans as

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99. Susan Lindt, *What's in a Name*, INTELLIGENCE J., Oct. 1, 2001, at 1; *see also* Amy Kover, *Big Banks Debunked*, Fortune.com, www.fortune.com (Feb. 21, 2000).

100. Thomas A. Stewart, *Where the Money Is*, FORTUNE, Sept. 3, 2001, at 153-57.

101. Robert Luke, *Battle for Wachovia: The Aftermath*, THE ATLANTA JOURNAL AND CONSTITUTION, Aug. 4, 2001, at F1.

102. *The Great League Table Debate*, *supra* note 93, at 116 ("As banks continue to scalle bank their lending commitments, credit-whether revolving or term-is going to become more scarce and the ability to provide it more valuable to clients.").

103. Pacelle, *supra* note 94.

104. Christa Fanelli, *Still Looking*, INVESTMENT DEALERS DIG., Apr. 9, 2001.

105. *The Great League Table Debate*, *supra* note 93, at 117.

106. Jathon Sapsford, *Fewer Banks Mean Costlier Credit Lines*, WALL ST. J., Mar. 14, 2001.

107. Lewis Braham, *A Rude Awakening for Go-Go Lenders*, BUS. WK., Apr. 30, 2001, at 124.

being underpriced,[108] and often are used as a loss leader to attract more profitable business.

Because of the consolidations, customers are concerned about appeasing the dwindling number of big commercial banks that can make larger bank loans.[109] Customers are worried that commercial banks may be less likely to lend to them in a liquidity crunch unless they demonstrate their loyalty by purchasing more products and services from their primary lenders.[110]

B. Paying to Play

Large investments banks such as Goldman Sachs and Morgan Stanley are discovering that market power is shifting with respect to securities underwriting services. Because of the Glass-Steagall restrictions, investment banks were protected from large commercial banks competing for underwriting business, thus limiting customers in their choice of securities underwriters.[111] Now it is increasingly necessary for investment banks to "pay to play."[112]

Requiring underwriters to lend to the customer in addition to underwriting the customer's securities is referred to as "pay to play." Many of the largest public companies are not granting underwriting to investment banks who do not also lend to them.[113] Increasingly in need of credit, customers are tired of investment banks unwilling to lend in exchange for highly profitable underwriting business.[114] As they parcel out lucrative underwriting transactions, customers are demanding that the securities underwriters also lend to them.[115] Similar behavior also occurs with issuances of asset-backed

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108. *The Great League Table Debate*, *supra* note 93, at 116.

109. McGeehan, *supra* note 9, at C1.

110. *Id.*

111. *See supra* text accompanying notes 10-13.

112. McGeehan, *supra* note 9, at C1.

113. Christopher O'Leary, *Solly's Big Climb*, INVESTMENT DEALERS DIG., Apr. 30, 2001 (Some issuers are demanding that the firms "give the loans in order to get underwriting mandates."); *The Great League Table Debate*, *supra* note 93, at 117.

114. *The Great League Table Debate*, *supra* note 93, at 118.

115. Gregg Wirth & Michelle Celarier, *Into the Crucible*, INVESTMENT DEALERS DIG., June 11, 2001 ("First Ford Motor Co., then Deutsche Telekom AG and Vodafone Group Plc demanded that investment bankers looking for underwriting mandates put their money on the table-or risk being left out of the deal flow."); *see also* Sapsford et al., *supra* note 88.

securities.[116] Investment banks are complaining that underwriting business is now going to commercial banks that will lend as well as underwrite securities.[117]

Two recent examples illustrate the trend. In June of 2001, Kraft Foods entered into an $8.6 billion initial public offering.[118] Although some 60 firms participated in the stock offering, both Merrill Lynch and Goldman Sachs, two of the premier securities underwriters, were not given their traditional roles in the IPO, principally because they were unwilling to participate in an earlier $9 billion syndicated loan for Kraft's parent company.[119] Merrill Lynch was cut out of the underwriting for a customer because the customer hired commercial banks as underwriters that had provided the client with more than $2 billion in credit.[120] Ford Motor Company, AT&T, Lucent Technologies, and Primedia, Inc. are also examples of customers that have publicly gone on record requiring their securities underwriters to lend as well.[121]

This convergence is wreaking havoc for investment banks with respect to their long term survival. Many are realizing that "pay to play" is becoming institutionalized and a normal part of doing business. In spite of protests to the contrary,[122] many have decided that merging with commercial banks may be inevitable.[123]

This development, at least at first blush, would appear to be the antithesis of tying. Here the customer attempts to tie its purchase of underwriting services with the underwriter's provision of credit. It is indicative, however, as to how important credit has become to customers. Less sophisticated borrowers may discover that they do not enjoy this power and that commercial

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116. Tempkin, *supra* note 68. *See also* Adam Tempkin, *S& P Release Negative Outlook for Goldman, Morgan Stanley, and Merrill*, ASSET SECURITIZATION REP., July 23, 2001 ("As large commercial banks continue to sue their ability to lend credit for the purpose of dominating the ABS league tables, investment banks that are not able to provide lines of credit to issuers are having difficulty matching the volume of business . . . .").

117. Frank Musero, *Pru Departs ABS Market*, PRIVATE PLACEMENT LETTER, Nov. 13, 2000.

118. Sapsford et al., *supra* note 88; Randall Smith & Suzanne McGee, *Banks' Lending Clout Stings Securities Firms*, WALL. ST. J., June 15, 2001, at C1.

119. McGeehan, *supra* note 9; Smith & McGee, *supra* note 118; *On Draft IPO, Goldman says no to Pay to Play*, INVESTMENT DEALERS DIG., Mar. 26, 2001, at 4-6.

120. McGeehan, *supra* note 9.

121. Smith & McGee, *supra* note 118. *On Draft IPO*, *supra* note 119, at 4-6.

122. Sapsford et al., *supra* note 88 (explaining in spite of merger pressure, Merrill Lynch, Lehman and Goldman Sachs "have consistently said that they want to remain independent").

123. *Id.* (discussing of need to have a balance sheet that will support lending).

banks are pushing them to use them as underwriters if they want to maintain their lending relationship.

C. Lending as a Competitive Weapon

Commercial banks view their lending business as an important competitive advantage to both retain current underwriting customers and also attract new ones.[124] Investment banks are already concerned about commercial banks using their lending power to get securities underwriting business.[125] Commercial banks have shown that they are willing to use their balance sheets to compete,[126] offering "big corporate loans as a sweetener to get lucrative underwriting deals."[127] It seems a short step however, before commercial banks will begin withholding credit in order to influence customers to underwrite securities through them.

Commentators generally anticipated that commercial banks would use their lending business to get underwriting business after the Glass-Steagall restrictions on securities underwriting were eliminated.[128] Lending to customers without selling other services has become less attractive for commercial banks.[129] Syndicated loans, for example, have helped open the way for commercial banks to enter into other types of business such as underwriting.[130] This advantage appears to be particularly helpful for obtaining debt underwriting engagements,[131] although the advantage for equity underwriting may be less obvious.[132]

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124. Julie Creswell, *Banking's Not-So-Sweet Weapon*, FORTUNE, Oct. 14, 2002, at 158. Tim Huber, *Banks Seek Underwriting OK*, CITY BUS., Oct. 24, 1997.

125. Schiffrin, *supra* note 91, at 86.

126. *Massive Profit, Minimal Risk*, NAT'L POST, July 18, 2001.

127. *Id.*

128. Schiffrin, *supra* note 91, at 86.

129. McGee, *supra* note 80, at C20.

130. Robert Lenzer, *Jimmy's List*, FORBES, Apr. 17, 2000, at 198.

131. Laura Santini, *Investment Banking's Star Crossed Year*, INVESTMENT DEALERS DIG., Jan. 7, 2002 ("[U]se of balance sheets on the part of commercial banking hybrids to win investment banking business, may have figure most prominently in debt markets . . . .").

132. Britt Tunick, *See Pay to Play Doesn't Pay?*, INVESTMENT DEALERS DIG., Dec. 17, 2001, at 1; *see also I-Grade League Tables May Overdo Commercial Bank Underwriting Role*, BONDWEEK, Jan. 7, 2002, at 4 (suggesting that commercials banks may not have made as much progress as indicated).

Commercial banks have not been bashful about using their "lending clout to land underwriting work."[133] For example, Chase is willing "to use its extensive lending relationships to muscle its way into stock-underwriting mandates."[134] Chase is also pitching its underwriting services both to potential and existing borrowing clients.[135] This willingness to lend will help the commercial banks obtain lucrative initial public offerings and other underwriting assignments.[136] To compete, investment banks are being required to offer credit lines,[137] in addition to its traditional role as a securities underwriter.[138] However, even if the investment banks wanted to expand their lending activities, they would still be at a competitive disadvantage with the commercial banks.[139] For example, investment banks do not have access to cheap deposits that can be lent at inexpensive interest rates.[140] Investment banks have a difficult time competing with commercial banks in the lending arena because commercial banks enjoy accounting advantages that allow them to offer loans cheaper than investment banks.[141] For example, commercial banks are not required to mark-to-market their bank loans on a daily basis as do investment banks.[142]

As the underwriting market has become more competitive, commercial banks have begun to enter into underwriting with not only the largest and most sophisticated financial institutions, but also with their smaller and less creditworthy borrowers, a potentially large securities underwriting market for

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133. Joanne Hart, *Pressure is on as Commercial Banks Flex Muscles*, THE EVENING STANDARD, Nov. 23, 2001, at 61; McGee, *supra* note 80; Christopher O'Leary, *S&P Negative Call*, INVESTMENT DEALERS DIG., July 23, 2001; Tempkin, *S&P Releases Negative Outlook*, *supra* note 115 (explaining that in the ABS area, "banks use their balance sheets and liquidity to lure clients").

134. McGee, *supra* note 80, at C20.

135. *Id.*

136. *Id.*

137. Emily Thornton, *Now Brokerage Have to "Pay (More) to Play*," BUS. WK., May 28, 2001, at 94.

138. *Morgan Stanley's Midlife Crisis*, BUS. WK., June 24, 2001, at 90, 91; Wirth & Celarier, *supra* note 115.

139. Thornton, *supra* note 137.

140. *The Great League Table Debate*, *supra* note 93, at 116. Even without cheap deposits, an investment bank such as Merrill Lynch should still be able to compete. Richard Melville, *Preferred Issues: Goldman, Merrill Bulk Up Even as They Opt Out*, THE AMERICAN BANKER, June 18, 2001, at 9.

141. O'Leary, *supra* note 133 (accounting advantages); Thornton, *supra* note 137, at 94; Wirth & Celarier, *supra* note 115; *but see* Gregg Wirth, *FASB Ruling Stirs Play-to-Play Plot*, INVESTMENT DEALERS DIG., Jan. 7, 2002 (some accounting advantages being eliminated).

142. McGeehan, *supra* note 9.

commercial banks.[143] Although a large commercial bank may have numerous underwriting engagements, it may have many more borrowers to whom it lends money. Chase Manhattan Bank, for example, is directing much of their underwriting business to their "existing non-investment grade customers."[144]

Given these pressures in the financial market, members of Congress have begun to look into the possibility of commercial banks tying services to the extension of credit.[145] In response to congressional concern, banking regulators are beginning to study the issue more carefully.[146] Although initially not finding any concerns, federal banking regulators have already begun to respond to congressional questions.[147] In addition, the General Accounting Office is also looking into the issue.[148]

Although current practices appear to be innocent of tying concerns, there is potential for commercial banks to step over the line. As competition sharpens with investment banks, commercial banks may be tempted to fully exert their competitive lending advantage. It is a short step between offering to lend to a customer as a sweetener to obtain an underwriting mandate and threatening to withhold credit if the customer does not place its underwriting with the commercial bank.

III. RETHINKING THE ANTITYING RULES

Commercial banks risk violating the antitying rules as they attempt to integrate their lending and underwriting activities. Aggressively marketing their underwriting capacities, commercial banks may overtly or inadvertently

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143. JOHNSON, *supra* note 1.

144. McGee, *supra* note 80.

145. Jathon Sapsford & Paul Beckett, *Linking of Loans to Other Business Has Perils for Banks*, WALL ST. J., Sept. 19, 2002, at A1.

146. *US Bank Regulators Review Credit Tying Allegations*, REUTERS MARKET NEWS, *at* http://biz.yahoo.com/rf/020913/financial_banks_tying_1.html (last visited Sept. 13, 2002) (on file with the University of Pittsburgh Law Review).

147. Letter from Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, and John D. Hawke, Jr., Comptroller of the Currency, to Rep. John D. Dingell, U.S. House of Representatives (Aug. 13, 2002) (on file with the University of Pittsburgh Law Review); Letter from Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, and John D. Hawke, Jr., Comptroller of the Currency, to Rep. John D. Dingell, U.S. House of Representatives (Oct. 16, 2002) (on file with the University of Pittsburgh Law Review).

148. Telephone Interview with Toni Gillich, Senior Analyst, Financial Markets and Community Investment, U.S. General Accounting Office (Nov. 22, 2002).

violate the BHCA antitying provisions as they encourage customers to use their underwriting services. As competition becomes more fierce between commercial banks and investment banks, commercials banks are less bashful about reminding customers of the importance of their being a profitable customer—suggesting that the commercial bank may be less likely to lend if the customer does not also purchase underwriting services.

In analyzing the BHCA antitying provisions in light of current conditions, commercial banks are stepping precariously close to liability. Regardless of their tying attempts, however, it may prove particularly difficult for plaintiffs to establish damages as courts weigh whether the plaintiff paid too much for the combined services to the commercial bank.

Congress has demonstrated its desire to level the playing field between commercial banks and investment banks with respect to securities underwriting. As commercials banks have quickly developed their underwriting capacity, they may enjoy a competitive advantage over investment banks that was not anticipated by Congress. The antitying provisions of the BHCA, however, may provide an important counterweight to this competitive advantage, ensuring that this playing field remains level.

A. Bank Antitying Provisions and Antitrust Law

Concerns about the anticompetitive effect of tying different products and services together have existed since the inception of antitrust law.[149] Demonstrating Congressional concerns over the issue, both the Sherman Act[150] and the Clayton Act[151] contain restrictions against tying.[152] Tying claims have also been brought under Section 5 of the Federal Trade Commission Act.[153] Because of the special relationships that commercial

149. For a general discussion of the restrictions against tying, see William M. Hannay & William A. Montgomery, *Tying Arrangements: Practice Under Federal Antitrust, Patent, and Banking Law*, 39-2nd CORP. PRAC. SERIES (BNA) (1997); HERBERT HOVENKAMP, ECONOMICS AND FEDERAL ANTITRUST LAW § 8 (student ed. 1985); HEBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE § 5 (4th ed. 1999); SPENCER WEBER WALLER, INTERNATIONAL TRADE AND U.S. ANTITRUST LAW § 1 (Jeffrey L. Kessler rev., West Group 1999); LAWRENCE A. SULLIVAN & WARREN S. GRIMES, THE LAW OF ANTITRUST: AN INTEGRATED HANBOOK § 7 (2000).

150. 15 U.S.C. § 1 (2000).

151. 15 U.S.C. § 14 (2000).

152. H.R. REP. NO. 63-627, at 10-13; S. REP. NO. 63-698, at 6-9 (1914).

153. 15 U.S.C. § 45 (2000).

banks enjoy with their customers, Congress has enacted specific federal antitying provisions under the BHCA.[154]

Congress enacted the BHCA[155] in response to worries that the Clayton and Sherman Acts were insufficient to curb the anticompetitive behavior of commercial banks and their affiliates. Congress was concerned that "because of the importance of the banking system to the national economy, adequate safeguards should be employed against undue concentration of control of banking activities."[156]

The BHCA generally regulates the activities of "banks."[157] The Federal Reserve Board was empowered to include bank holding companies and their nonbank subsidiaries as part of the regulation.[158] The BHCA is enforced by the attorney general who may "institute proceedings in equity to prevent and restrain" violations of the statute.[159] Remedies and damages under the BHCA include civil penalties,[160] private treble-damage actions,[161] and suits for injunctive relief by either the U.S. government or by private parties.[162]

In 1970, Congress amended the BHCA to expressly regulate activities of commercial banks that tie products or services together with the extension of credit. These are commonly referred to as the "antitying" provisions now

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154. For a history of the Bank Holding Company Act and the Amendments, see *Legislation Note: The Bank Holding Company Act of 1970*, 39 GEO. WASH. L. REV. 1200 (1971). For a discussion of the policy concerns, see Arthur D. Austin & Elinor Harris Solomon, *A New Antitrust Problem: Vertical Integration in Correspondent Baning*, 122 U. PA. L. REV. 366, 390 (1973); Joseph C. Chapelle, *Section 1972: Augmenting the Available Remedies for Plaintiffs Injured by Anticompetitive Bank Conduct*, 60 NOTRE DAME L. REV. 706 (1985) (discussing policies underlying antitying provisions); Earl W. Kintner & Joseph P. Bauer, *Competition at the Teller's Window?: Altered Antitrust Standards for Banks and Other Financial Institutions*, 35 KAN. L. REV. 657 (1987); Daniel R. Fischel et al., *The Regulation of Banks and Bank Holding Companies*, 73 VA. L. REV. 301, 329-330 (1987); John A. Weinberg, *Tie-In Sales and Banks*, 82 FED. RES. BANK OF RICHMOND ECON., Spring 1996, at 1.

155. 12 U.S.C. §§ 1841-1850 (2000).

156. S. REP. NO. 1095, 84-1095, pt. 2, *reprinted in* 1956 U.S.C.C.A.N. 2482, 2482.

157. 12 U.S.C. § 1841(c) (2000). The definition defines a "bank" as:

> [a]ny institution organized under the laws of the United States, any State of the United States, the District of Columbia, any territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands which both (i) accepts deposits that the depositor has a legal right to withdraw on demand, and (ii) engages in the business of making commercial loans. *Id.*

158. 12 C.F.R. § 225.7(a) (2002).

159. 12 U.S.C. § 1973 (2000).

160. 12 U.S.C. § 1972(2)(F) (2000).

161. 12 U.S.C. § 1975 (2000); Kabealo v. Huntington Nat'l Bank, 17 F.3d 822, 826 (6th Cir. 1994), *cert. denied*, 513 U.S. 812 (1994); Lancianese v. United Bank of Mt. Hope, 783 F.2d 467 (4th Cir. 1986).

162. 12 U.S.C. § 1976 (2000).

found in Section 1972 of Title 12 of the U.S. Code ("Section 1972").[163] The keystone provision provides that "[a] bank shall not in any manner extend credit . . . on the condition or requirement . . . that the customer shall obtain some additional credit, property, or service from such bank other than a loan, discount, deposit or trust service."[164] Importantly, the statute also includes products or services that might be offered by a subsidiary or affiliate of the commercial bank.[165] This restriction is critical in that most commercial banks appear to be offering underwriting services through a securities affiliate.[166]

Courts have generally identified that a claimant must show the following to establish a violation of the antitying provisions of the BHCA: (1) a tying arrangement between two products or services; (2) the practice was anticompetitive; (3) a benefit to the bank; (4) damage to the claimant; and that (5) the tying arrangement was not subject to an exception.[167]

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163. Bank Holding Company Act Amendments of 1970, Pub. L. No. 91-607, § 106(b), 84 Stat. 1760, 1766-67 (codified as amended at 12 U.S.C. § 1972(1) (1988)). In addition to the antitying provisions, the amendments also prohibited reciprocal and exclusive dealing arrangements. *Id.*

164. 12 U.S.C. § 1972(1)(A) (2000). The entire provision reads as follows:

> A Bank shall not in any manner extend credit, lease or sell property of any kind, or furnish any service, or fix or vary the consideration for any of the foregoing, on condition or requirement—
>
> (A) that the customer shall obtain some additional credit, property, or service from such bank other than a loan, discount, deposit or trust service;
>
> (B) that the customer shall obtain some additional credit, property, or service from a bank holding company of such bank, or from any other subsidiary of such bank holding company;
>
> (C) the that customer provide some additional credit, property, or service to such bank, other than those related to and usually provided in connection with a loan, discount, deposit, or trust service;
>
> (D) that the customer provide some additional credit, property, or service to a bank holding company of such bank, or to any other subsidiary of such bank holding company; or
>
> (E) that the customer shall not obtain some other credit, property, or service from a competitor of such bank, a bank holding company of such bank, or any subsidiary of such bank holding company, other than a condition or requirement that such bank shall reasonably impose in a credit transaction to assure the soundness of the credit.

165. § 1972(1)(B) ("from a bank holding company of such bank, or from any other subsidiary of such bank/holding company").

166. *See supra* text accompanying note 69.

167. For a general discussion of the elements that a claimant must show, see James L. Rigelhaupt, Jr., *Annotation: What Constitutes Violation of Provisions of Bank Holding Act Prohibiting Tying Arrangements*, 74 A.L.R. Fed. 578 (1985); Daniel Aronowitz, Note, *Retracing the Antritrust Roots of Section 1972 of the Bank Holding Company Act*, 44 VAND. L. REV. 865 (1991); Chapelle, *supra* note 154; Robert F. Finke & Daniel G. Hildebrand, *Antitrust Compliance in the Banking Industry*, C880 ALI-ABA 179 (1994).

B. *Elements of a Tying Violation*

Each of the elements of a tying violation should be analyzed with respect to commercial banks relatively recent entry into securities underwriting. On a superficial level, commercial banks appear to be crossing the antitying line as they compete for underwriting engagements.

1. *Tying Arrangement*

To constitute a violation of the BHCA, the borrower is required to show a tying arrangement. Under this analysis, the borrower needs to show that to obtain credit from the commercial bank, the borrower was required to purchase another product or service from the commercial bank such as engaging the commercial bank as its underwriter.

Actually finding such a tie, however may be difficult. Banks are aware of the antitying provisions and there appear to be no examples of contractual requirements in loan documents to tie the provision of credit to underwriting services. Plaintiffs may be more successful, however, in arguing that such a tie is implied as banks threaten to reduce or cut off credit if a customer fails to purchase additional services. Even if such a tie is found, commercial banks may argue that they are providing "financing" for their customers, whether it be through lending or underwriting, and that only one product or service is being offered.

Express Tie. The most compelling situation for establishing a tying arrangement would occur if the loan documentation required the lender to also be the underwriter for a customer's securities offerings. It would be unusual however, for a commercial bank to be so reckless and aggressive as to make it an express contractual requirement.

Commentators have said that a borrower's voluntary agreement to tie two products together should not create liability under the BHCA antitying provisions.[168] General antitrust law is also clear that if a customer is not expressly required to tie the two products together, and is free to take or refuse

168. C. BLAINE, FEDERAL REGULATION OF BANK HOLDING COMPANIES § 12.16 (1973) ("It seems clear for a number of reasons that such [voluntary] tying effects are not prohibited . . . , but principally because by definition they are voluntary on the part of the customer and not party of any condition or requirement of the bank.").

one or either of the two products, no tie exists.[169] In the absence of evidence of a written contractual requirement establishing a tie, the plaintiff's burden of establishing an illegal tying arrangement is more difficult.

Extending this analysis to underwriting, it could be argued that so long as the commercial bank did not expressly require the underwriting to be done with the commercial bank, there could not be a violation. There appears to be no examples of a loan term sheet or loan documentation that has required a customer to use its commercial bank as its securities underwriter. Without such express language, the customer would need to establish that, in the language of general antitrust law, it was "coerced" into accepting the tied product, even though such a requirement was not a contractual term.

Implied Tie. Although there appears to be no BHCA case law to this effect, it has been suggested that an implied or coerced tie should also violate the BHCA antitying provisions.[170] General antitrust law supports the interpretation that coercion can constitute a tie, even if it is not an express tie.[171] In an implied tie-in, the borrower understands from the commercial bank that if it does not use the commercial bank as its securities underwriter, the commercial bank may not extend or renew the customers loans or credit extensions.

In analyzing the public statements and positions of large commercial banks, they appear to be on the verge of tying the provision of credit to their underwriting services. Commercial banks have been very aggressive in publicizing that a customer should give the commercial bank other non-lending business if it wants the commercial bank to continue its lending relationship.

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169. HOVENKAMP, *supra* note 149, at § 10.4a ("If a customer for item A is free to take or refuse item B as he pleases, there is no tie-in and there should be no liability.").

170. BLAINE, *supra* note 168, at § 12.16 ("While . . . it would be difficult to provide [an implied] condition or requirement, . . . assuming that the exact discussion [implying a condition] could be proved, might tend to indicate that a condition or requirement was part of the arrangement . . . [Banks should] avoid transactions . . . creating factual circumstances from which a court might infer an impliedly prohibited transaction.").

171. WILLIAM C. HOLMES, ANTITRUST LAW HANDBOOK 347-49 (1996) (Tie can result "because this was a condition formed upon him . . . by the practical economics of the arrangement."); HOVENKAMP, *supra* note 145, at § 10.4a (discussing ties through coercion by contract, condition or understanding); STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST LAW 286 (1993) ("A sale may be tied, however, even though the buyer is not legally obligated to purchase the tied product in order to obtain the tying good"); *see also* United Shoe Mach. Corp. v. United States, 258 U.S. 451, 458 (1922) (business realities can "practically compel" a tie).

Commercial banks are already limiting their lending to customers that do not purchase additional services from the commercial bank.[172] In general, commercial banks are not lending money "in the absence of a relationship with the borrower-that is, securities or advisory business."[173] Commercial banks are analyzing the overall profitability of a customer when making a loan, not just focusing on the profitability of the loan itself.[174] As technology allows commercial banks to track their relationship with a customer, it will become even easier to determine if a customer is profitable for the commercial bank to lend to.[175]

Commentators have noted that commercial banks appear to have gone beyond using cheap lending as a loss leader in order to land more lucrative securities underwriting mandates. For example, in the asset backed securitization area, commercial banks already appear to be tying their lending activities to their underwriting mandates for asset based securities transactions: "Commercial banks, which have begun to make more inroads into investment banking with the demise of the Glass-Steagall act, are more willing to oblige, explicitly linking their investment banking business to their lending arms, and using the latter as leverage for winning mandates."[176]

It is likely that commercial banks will continue to exploit this competitive advantage. Even though the commercial bank's language is strong, the commercial bank's actions should not necessarily be viewed as a classical tie that was intended to be restricted by the statute. What the commercial banks appear to be arguing is that they can no longer afford to make inexpensive loans to their customers. If the customer desires inexpensive bank loan financing, then it will have to compensate the commercial bank in other ways—perhaps through purchasing additional products or services, such as underwriting, that have better margins and less risk for the commercial bank.

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172. Alissa Leibowitz, *Citi May Limit Syndications to its Existing Customers*, AMERICAN BANKER, Feb. 7, 2001, at 2 (describing that Citigroup, J.P. Morgan Chase and Bank of America are all focusing on whether the customer is profitable overall—Citigroup is "growing less tolerant to companies who want it for lending but nothing else."); Joseph Segar, *Making Good on Past Threats*, BANK LOAN REPORT, July 16, 2001. Bank of America, Bank One are both dropping customers that do not use other services that the bank offers. *Id.*

173. *The Great League Table Debate*, *supra* note 93; Segar, *supra* notes 90 and 172.

174. Schiffrin, *supra* note 91, at 86 ("looking at overall picture for each client").

175. Segar, *supra* note 172.

176. Tempkin, *supra* note 68.

It is probable that the commercial banks would lend to those customers that they have dropped if the price was right. The price of that lending, however, would probably be much higher to compensate the commercial banks for their efforts and for the risks that they are assuming. As expressed above, pricing on many syndicated loans is so tight that the commercial banks appear to be using it as a loss leader.[177] As the lending market evolves and traditional lending pricing and analysis proves unprofitable, it is probable that the rest of the market will follow the lead of Bank of America and Bank One by rationalizing the returns they should be earning from their lending activities.

The intent of the antitying provisions is clearly not to force commercial banks to offer lending at a rate that does not adequately compensate them, rather it is aimed at anticompetitive behavior. Expressing an unwillingness to lend at an unprofitable rate and level, without some form of additional compensation, should not be viewed as anticompetitive, but instead as a normal part of the business cycle.

One Product versus Two. Assuming there is a tie in form between the loan and the underwriting services, there may not be a tie in substance if there are not "separate products."[178] Although there appears to be no BHCA case law discussing this "separate product" doctrine, it could be argued that lending and underwriting are not separate products; rather, the commercial bank was providing overall financing to its customers, and there should be no artificial separation between lending and underwriting for the purpose of the BHCA antitying provisions. In viewing the substantial changes occurring in the capital markets, commercial banks themselves may not view these as separate services.

The lending and securities underwriting divisions in commercial banks are beginning to blur.[179] Commercial banks are now trying to offer financial

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177. *See supra* text accompanying note 176.

178. HOVENKAMP, *supra* note 149, at § 10.5 ("A tying arrangement does not exist unless the defendant bundles 'separates' tying and tied products"); STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST LAW 287 (1993) ("[T]ied sales involve products that are really separate."); WILLIAM C. HOLMES, ANTITRUST LAW HANDBOOK 341 (2001) ("An important threshold in any tying case is the requirement that the purportedly tied items entail separate products or services"); *see also* United Shoe Mach. Corp. v. United States, 258 U.S. 451, 458 (1922) (explaining that business realities can "practically compel" a tie).

179. *The Great League Table Debate*, *supra* note 93, at 116 ("[T]he lending and securities businesses of most major institutions are no longer separate and distinct divisions.").

solutions to a customers' needs, as opposed to just pitching one particular financial product such as a loan or a bond underwriting.[180] For example, Salomon Brothers is combining its debt underwriting group with Citibank's lending group,[181] treating them essentially as different solutions for helping to finance a customer. Salomon Brothers has been successful lending to foreign customers by combining its "lending and bank underwriting."[182]

As part of this effort, Salomon Brothers is leveraging its underwriting business from Citibank's lending relationships.[183] The product or service offered by Citibank and its affiliate Salomon Brothers is not a loan or an underwriting engagement; instead they enable customers to obtain the financing they need to run their business, regardless of the source of the financing.

It could be argued, however, that lending money is too distinct from securities underwriting to be considered the same product or service, even if they both constitute financing. The real question, however, may be from what distance one views the service. For example, commercial bankers would question whether unsecured lending is the same service as asset-based lending. They would argue that although both deal with providing credit, credit analysis and terms and risks are completely different from each other. In a similar manner, lending and securities underwriting also both deal with helping a customer raise financing in order to operate its business.

General antitrust case law may run counter to this argument. General antitrust case law provides that separate products depend upon whether "the tying item is commonly sold separately from the tied item in a well functioning market."[184] Under this scenario, it would be difficult to argue that lending and underwriting were a single product, given that for numerous decades these products have been offered separately. However, commentators acknowledge that this issue is complicated because "products and services can be marketed in such a manner as to seemingly blend together into a single integrated item."[185] As can already be seen in the capital markets, it may

180. *Id.*
181. O'Leary, *supra* note 113.
182. *Id.*
183. *Id.*
184. HOVENKAMP, *supra* note 149, at § 10.5a.
185. HOLMES, *supra* note 178, at 341.

become an antiquated practice for a firm to only offer underwriting as opposed to lending, or vice versa.

General antitrust law also provides however, that they still might not be characterized as separate products if they can either be viewed as substitutes or the economic equivalent for each other.[186] This principle would be reinforced by commercial banks efforts to integrate lending and underwriting as part of the financing that a newly deregulated financial service firm provides to a customer. Courts should not find a tie if the products are considered to be "functionally and economically part of the same overall product or service."[187]

2. *Anticompetitive Practice*

Courts have generally required a plaintiff to show an *anticompetitive* tying arrangement in order for it to constitute a violation of the antitying provisions. This standard is unique to the BHCA and sets a much higher standard of behavior for commercial banks. An anticompetitive tying arrangement can be shown by demonstrating that a practice is "anticompetitive in nature" or an "anticompetitive practice."[188] The courts have not required a plaintiff, however, to show an anticompetitive effect, or appreciable market share in the market for the tied services or products.[189] Showing that an investment bank's behavior had an anticompetitive effect is a much higher standard to reach for a plaintiff.

Compared to the Sherman and Clayton Acts, the BHCA "focus[es] on the interests of the individual credit consumer, rather than on 'competition' at large. The antitying provisions broadly proscribes tying . . . without requiring

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186. HOVENKAMP, *supra* note 149, at § 10.5a.

187. HOLMES, *supra* note 178.

188. Johnstone v. First Bank Sys., Inc., 947 F. Supp. 1220, 1225 (N.D. Ill. 1996); Palermo v. First Nat'l Bank & Trust Co. of Okla. City, 894 F.2d 363, 368 (10th Cir. 1990); Kenty v. Bank One, Columbus, N.A., 92 F.3d 384, 394 (6th Cir. 1996).

189. *See* Doe v. Norwest Bank Minn., N.S., 107 F.3d 1297, 1305 (8th Cir. 1997); S & N Equip. Co. v. Casa Grande Cotton Gin Fin. Co., 97 F.3d 337, 346 (9th Cir. 1996); Dibidale of La., Inc. v. Am. Bank & Trust Co., New Orleans, 916 F.2d 300, 305 (5th Cir. 1990); Bruce v. First Fed. Sav. & Loan Assoc. of Conroe, Inc., 837 F.2d 712, 718 (5th Cir. 1988); Amerifirst Props., Inc. v. Fed. Deposit Ins. Corp., 880 F.2d 821, 826 (5th Cir. 1989); Gage v. First Fed. Sav. & Loan Assoc. of Hutchinson, Kan., 717 F. Supp. 745, 752 (D. Kan. 1989); JST Properties v. First Nat'l Bank of Glencoe, 701 F. Supp. 1443, 1449 (D. Minn. 1988).

proof of economic power or a significant effect on commerce."[190] Congress acknowledged the unique nature of the commercial banking industry given its important role in the economy when it passed the BHCA.[191] Congress also recognized the inherent difficulties in proving an antitrust violation in the commercial banking area.[192]

In comparison, to establish a violation under the Sherman Act, the plaintiff must show an anticompetitive effect emanating from a tying arrangement. To prove an anticompetitive effect, the plaintiff must demonstrate: that the defendant possesses market power over the tying product to force the purchase of the tied product and that "a substantial volume of commerce is foreclosed thereby."[193]

Courts have distinguished between "anticompetitive effects" and "anticompetitive practices." Specifically, the 10th Circuit Court of Appeals reasoned that a commercial bank's dominance or control over the tying product market or over a substantial volume of commerce would constitute anticompetitive effects.[194] Practically speaking, these are the requirements for a general antitrust case. The court goes on to describe that in order to prove an anticompetitive practice, the plaintiff must show the practice either results in unfair competition or lessens competition.[195]

For plaintiffs filing suit under the BHCA instead of the Sherman Act, having to show an anticompetitive practice instead of an anticompetitive effect is a significant distinction. The nature of the elements to be proven in establishing an anticompetitive practice is far easier to prove than anticompetitive effects. One court discussed the reasons for the less stringent standard under the BHCA:

> In enacting the antitying provision of the BHCA, Congress recognized that tying arrangements in the banking industry generally involve such small dollar amounts that they do not justify expensive and time-consuming antitrust litigation. Congress also

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190. Hannay & Montgomery, *supra* note 149, at A-49.

191. *S & N Equip*. Co., 97 F.3d at 346; *Dibidale*, 916 F.2d at 305; *JST Properties*, 701 F. Supp. at 1449; S. REP. NO. 91-1084, 2d Sess., *reprinted in* 1970 U.S.C.C.A.N. 5519, 5558.

192. *See JST Properties*, 701 F. Supp. at 1449 (quoting, Naegele, *The Antitying Provision: Its Potential is Still There*, 100 BANKING L.J. 138, 143 (1983)).

193. Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 13-16 (1984).

194. *See Palermo*, 894 F.2d at 368; *Doe*, 107 F.3d at 1305; Davis v. First Nat'l Bank of Westville, 868 F.2d 206, 208 (7th Cir. 1989).

195. *Palermo*, 894 F.2d at 368; *Doe*, 107 F.3d at 1305.

> recognized the difficulties in establishing an antitrust violation, since it is doubtful whether a bank customer could adduce sufficient evidence of the bank's market power and the effect on interstate commerce to recover under the Sherman Act. Thus, even if evidence of market power and the effect on interstate commerce are insufficient to state a cause of action under the Sherman Act, a litigant can still recover under Section 1972 of the Bank Holding Company Act.[196]

In a situation where the borrower must use the commercial bank as its underwriter in order to receive credit, the different standards between the Sherman Act and the BHCA are clear. First, under the Sherman Act, the plaintiff must demonstrate that the commercial bank has substantial power in the loan market (tying product) to force the borrower to accept the commercial bank as its underwriter (tied service). Second, the plaintiff must establish that the commercial bank's power in the loan market caused other lenders to be unable to compete in that market.

In contrast, to establish a tying violation under the BHCA, a plaintiff is only required to show that the antitying arrangement was an anticompetitive practice.[197] As such, a plaintiff would only need to prove that requiring the borrower to use the commercial bank as its underwriter as a condition to obtaining credit from the commercial bank is a tying arrangement, and the tying of the loan and the underwriting is anticompetitive in nature.[198] The second requirement is demonstrated by showing that the tying arrangement was intended to be anticompetitive or that the arrangement could lessen competition.[199] Therefore, in order to show that the tying arrangement was anticompetitive in nature, a plaintiff would only need to demonstrate that there were other financial institutions willing to underwrite a customer's securities.

3. *Benefit to the Bank*

The plaintiff must prove a benefit to the commercial bank from the sale of the tied product or service to the borrower when making his or her claim

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196. *See JST Properties*, 701 F. Supp. at 1449 (quoting, Naegele, *The Antitying Provision: Its Potential is Still There*, 100 BANKING L.J. 138, 143 (1983) (footnotes omitted)).

197. *Palermo*, 894 F.2d at 368; Kenty v. Bank One, Columbus, N.A., 92 F.3d 384, 394 (6th Cir. 1996); Johnstone v. First Bank Nat'l Ass'n, No. 95 C 2008, 1998 WL 565193 at 5 (N.D. Ill. Aug. 31, 1998).

198. *Palermo*, 894 F.2d at 368; *Kenty*, 92 F.3d at 394.

199. *Palermo*, 894 F.2d at 368 (10th Cir. 1990); *Doe*, 107 F.3d at 1305.

under the BHCA.[200] There is a distinction, however, "between anticompetitive benefits and the ordinary benefits derived from the protection of a bank's security in a customer loan."[201] The type of benefit referred to in the antitying statute is "one which results not from the legitimate protection of an investment, but from a 'misuse of the economic power of a bank.'"[202]

Where a banking practice is shown to protect the commercial bank's investment interest, courts have held that this is not a benefit to the bank under the BHCA.[203] Several cases have held various conditions legitimate to protect a commercial bank's interest.[204] One court has gone beyond discussing the protection of the commercial bank's investment interest.[205] In *Gage*, for instance, the commercial bank required the customer to grant the commercial bank an option to purchase a portion of the plaintiff's building.[206] The court held that the purchase of a portion of the building at the customer's expense was a benefit to the bank.[207] Further, the commercial bank did not need any additional protection for the loan. Additionally, the option to purchase a portion of the building did not give the commercial bank any greater protection.

The large underwriting fees that commercial banks are already earning would suggest that a commercial bank would benefit from the practice of tying

200. Swerdloff v. Miami Nat. Bank, 584 F.2d 54, 59 (5th Cir. 1978); McCoy v. Franklin Sav. Assoc., 636 F.2d 173 (7th Cir. 1980); Rae v. Union Bank, 725 F.2d 478 (9th Cir. 1984); Parsons Steel, Inc. v. First Ala. Bank, N.A., 679 F.2d 242, 245 (11th Cir. 1982); Cont'l Ill. Nat. Bank & Trust Co. v. Stanley, 585 F. Supp. 1385 (N.D. Ill. 1984). *See also* James L. Rigelhaupt, Jr., J.D., Annotation, *What Constitutes Violation of Provisions of Bank Holding Company Act Prohibiting Tying Arrangements*, 74 A.L.R. Fed. 578, § 4(c) (1985).

201. Continental Bank of Pa. v. Barclay Riding Academy, Inc., 459 A.2d 1163, 1170 (N.J. 1983).

202. *Id.* (quoting *Swerdloff*, 584 F.2d at 59).

203. *See Parsons Steel, Inc.*, 679 F.2d at 246; Pappas v. NCNB Nat'l Bank of N.C., 653 F. Supp. 699, 706 (M.D. N.C. 1987); New England Co. v. Bank of Gwinnett County, 891 F. Supp. 1569, 1575 (N.D. Ga. 1995).

204. Bieber v. State Bank of Terry, 928 F.2d 328 (9th Cir. 1991) (requiring officers of corporation to personally guarantee loan of corporation); *Palermo*, 894 F.2d 363 (requiring officers to personally guaranty loan of corporation); Davis v. First Nat'l Bank of Westville, 868 F.2d 206 (7th Cir. 1989) (requiring debtor to provide a business liquidation service); Alpine Elec. Co. v. Union Bank, 776 F. Supp. 486 (W.D. Mo. 1991) (finding that act of bank in using money in depositor's checking account to reduce debt of related corporation not actionable.).

205. *See* Gage v. First Fed. Sav. & Loan Ass'n of Hutchinson, Kan., 717 F. Supp. 745, 754 (D. Kan. 1984).

206. *Id.*

207. *See id.*

credit to an underwriting engagement.[208] The fees that could be earned from an underwriting engagement are what drives the commercial bank to offer underwriting services in the first place. An underwriting mandate can generate millions of dollars of fees to a commercial bank.

It would be difficult to argue, based on the case law, that even though the commercial bank did benefit from the underwriting fees, that its real motivation in tying the underwriting services was to protect its investment in the customer. There would appear to be little reason why a customer would be better served, or perhaps strengthened, by the commercial bank acting as the underwriter versus another investment bank. Although the customer will be strengthened economically by raising money through issuing securities, that result could be achieved by using an underwriter other than the commercial bank.

4. Damages

A borrower must show that "damages flow[ed]"[209] as a result of the product being tied to the extension of credit in order to recover damages (but not necessarily injunctive relief) under the antitying provisions.[210] However, no cases appear to describe how to calculate damages for a violation of the BHCA antitying provisions. Therefore, since the wording of the damages provision in the BHCA is nearly identical to the language contained in the Clayton Act, it would be reasonable to look to the analysis under the Clayton Act.[211] The Forth Circuit explained the criteria necessary to prove damages under the antitying provisions of the Clayton Act:

> [I]njury resulting from a tie-in must be shown by establishing that payments for both the tied and the tying products exceeded their combined fair market value . . . Unless the fair market value of both the tied and tying products are determined and an overcharge in the complete price found, no injury can be claimed; suit, then, would be foreclosed.[212]

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208. *See supra* text accompanying notes 83-87.

209. Sterling Coal Co., Inc. v. United Am. Bank, 470 F. Supp. 964, 965 (E.D. Tenn. 1979).

210. *See* Swerdloff v. Miami Nat. Bank, 584 F.2d 54 (5th Cir. 1978); Costner v. Blount Nat. Bank, 578 F.2d 1192 (6th Cir. 1978). For a discussion of damages under the BHCA, see Frederick A. Nicoll & Robert W. Delventhal, *The Antitying Provisions of the Bank Holding Company Act: Lenders Beware*, 109 BANKING L.J. 4, 18-22 (1992); Rigelhaupt, *supra* note 200, at § 4[e] (1985).

211. *Compare* 12 U.S.C. § 1975 (2001), *with* 15 U.S.C. § 15(a) (2001).

212. Kypata v. McDonald's Corp., 671 F.2d 1282, 1285 (4th Cir. 1982), *cert denied*, 459 U.S. 857

According to this analysis, a plaintiff would combine the cost on a net present value basis of the bank loan and the underwriting fees separately. A plaintiff would not be successful in merely showing that the commercial bank offered expensive underwriting services if the commercial banking loan was sufficiently inexpensive to offset the higher cost.

The cost of the loan could probably be calculated by comparing on a net present value basis how much more (or less) interest, fees, and other expenses the borrower might have paid under the loan in question versus a loan that it could have obtained from another commercial bank. The calculation of the cost of the underwriting fees paid to an underwriter could also be calculated in a similar manner.

As explained above, one of the impediments to investment banks offering loans and underwriting services as a package has been the low margins and costs involved in lending.[213] In calculating damages, a court would need to take into account the interest cost savings that a customer would benefit by receiving a competitively or below market priced loan against the fees and commissions that the customer would pay the commercial bank on an underwriting engagement.

5. Traditional Banking Practice Exception

Even if a plaintiff can establish that a commercial bank had expressly tied the purchase of a product or service from the commercial bank to the extension of credit, there may still be no liability if the tied service or product constitutes a traditional banking practice. In addition, if liability is predicated under subsection (1)(C) of Section 1972, it does not constitute an unusual banking practice.[214] It could be argued that the provision of underwriting securities may constitute a traditional banking practice from current market practice and perhaps from a historical perspective.

(1982); *see also* Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir.), *cert. denied*, 405 U.S. 955 (1972). For a general discussion of damages under the Clayton Act for a violation of the antitying provisions, see SPENCER WEBER WALLER & JEFFREY L. KESSLER, INTERNATIONAL TRADE AND U.S. ANTITRUST LAW 4-39 (West Group 2002).

213. *See supra* text accompanying notes 139-42.

214. 12 U.S.C. § 1972(1)(c).

Traditional Banking Practice. The intention of the BHCA antitying provisions was not to prohibit transactions and relationships dealing with traditional banking practices.[215] The exception emerged from the wording of the statute stating that the antitying prohibitions will not cover tied products including *"a loan, discount, deposit or trust service*."[216] In other words, there are certain types of products or services that can be tied to the provision of credit, such as requiring the customer to maintain his checking account at the bank, without creating liability under the statute.

As such, courts have declined to limit the traditional banking practice exception to "a loan, discount, deposit or trust service." In *Flags I, Inc. v. Boston Five Cents Savings Bank*,[217] the court clarified the use of the traditional banking practice exception.[218] The court explained that the drafters of the statute were not satisfied with the statute because it prohibited tying arrangements that were not anticompetitive.[219] Therefore, the statute was amended to allow legitimate banking practices with no anticompetitive effects.[220]

Courts have also tried to develop an expansive reading of the traditional banking practice exception. One court explained that a too narrow reading of the exception would be inappropriate: "[T]hey would preclude many newly established banking practices which serve legitimate banking interests without adversely affecting competition."[221] If the exceptions were so construed they would have a negative impact on the lending industry in particular because of

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215. *See* B.C. Recreational Indus. v. First Nat'l Bank of Boston, 639 F.2d 828, 832 (5th Cir. 1981); Sanders v. First Nat'l Bank & Trust Co. in Great Bend, 936 F.2d 273, 278 (6th Cir. 1991); Clark v. United Bank of Denver Nat'l Ass'n, 480 F.2d 235, 238 (10th Cir. 1973); Pappas v. NCNB Nat'l Bank of N.C., 653 F. Supp. 699, 705 (M.D. N.C. 1987); Alpine Elec. Co. v. Union Bank, 776 F. Supp. 486, 489 (W.D. Mo. 1991); Libby v. Firstar Bank of Sheboygan, 47 F. Supp. 2d 135, 139 (D. Mass. 1999); Flags I, Inc. v. Boston Five Cents Sav. Bank, 831 F. Supp. 928, 936 (D.N.H. 1993).

216. 12 U.S.C. § 1972(1)(A) (emphasis added).

217. *Flags I*, 831 F. Supp. at 936.

218. The exception involved a claim under the Home Owner's Loan Act, 12 U.S.C. § 1464(q)(1) (2001). The Home Owner's Loan Act is considered to be the savings association equivalent of the BHCA and therefore its analysis should be applicable to the BHCA. *See also Flags I*, 821 F. Supp. at 934; Integon Life Ins. Co. v. Browning, 989 F.2d 1143, 1150 (11th Cir. 1993); Bruce v. First Fed. Sav. & Loan Ass'n of Conroe, Inc., 837 F.2d 712, 716 (5th Cir. 1988).

219. *Flags I*, 831 F. Supp. at 934.

220. *Id.* at 935.

221. *Id.* at 937.

the need to develop creative ways for the lender to loan to the customer while still protecting its interest.[222]

The Flags' court explained further that instead of determining whether the arrangement was common in the banking industry, courts should broadly look to the effect of the arrangement.[223] Additionally, the court made it clear that an overly narrow definition of the traditional banking practice exception was not appropriate. The court explained that a more appropriate approach was to interpret the exception in light of the legislative purpose of the antitying provision.[224] Ultimately, the court found there needed to be: (1) an unusual banking practice, (2) a tying arrangement and (3) a benefit to the commercial bank.[225]

The current activities of U.S. commercial banks as securities underwriters could be probative that underwriting is a traditional banking practice. As shown above, U.S. commercial banks, or their affiliate subsidiaries, already represent four of the top fifteen most active underwriters in the United States, in spite of the artificial legal constraints that, until recently, were imposed on them by Glass-Steagall.[226] Although in execution, both underwriting and lending are quite different activities, they both serve a financial intermediation purpose that is well served by commercial banks. Both are concerned with helping customers raise money.

The securities activities of foreign banks, unrestrained by Glass-Steagall in the past, is evidence that commercial banks consider securities underwriting a traditional banking practice.[227] In a review of underwriting activity in the United States by *Investment Dealers Digest*, foreign commercial banks were shown to be active participants in the securities underwriting industry. For example, in the U.S. domestic rankings for debt and equity offerings for the year 2000, the following foreign companies were all ranked among the top 15 securities underwriters: Credit Suisse First Boston, a subsidiary of Credit Suisse Bank, Deutsche Banc, UBS Warburg, a subsidiary of UBS AG, and

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222. *See id.*
223. *Id.* at 936.
224. *See id.*
225. *See id.*
226. *See supra* text accompanying note 78.
227. McGeehan, *supra* note 9 ("Before these combinations, the only commercial banks that owned major investment banks were foreign.").

ABN AMRO.[228] These rankings, however, do not take into account the more specialized and international underwriting activities of foreign commercial banks.[229]

Prior to Glass-Steagall, it was common for commercial banks to underwrite a customer's securities as well as lend the customer money.[230] In fact, commercial banks probably viewed their role as raising money for the customer in any number of ways, whether it be through lending or underwriting securities.

Unusual Banking Practice. If the questioned tying relationship violates Section 1972 (1)(c) of Title 12,[231] then the unusual banking practice element appears to be a requirement Although possible, it is unlikely that this provision would apply to a tie involving the extension of credit and underwriting. According to case law, a traditional banking practice can not also be an unusual practice.[232] Courts have considered the opinions of banking experts as well as the individuals involved in such transactions in determining if a banking practice is unusual.[233] As discussed above, given the large amount of securities underwriting activities performed by commercial banks or their affiliates currently, the practice should not be considered unusual.[234]

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228. *Domestic Rankings*, INVESTMENT DEALERS DIG., Jan. 8, 2001.

229. In addition to the previously listed foreign commercial banks, Barclays Capital, an affiliate of Barclays Bank, BNP Paribas, Royal Bank of Scotland Group, an affiliate of the Royal Bank of Scotland, and CIBC World Markets, a subsidiary of Canadian Imperial Bank of Commerce, Societe Generale, Banco Commercial Portugues, Dresdner KB, an affiliate of Dresdner Bank, Westdeutsche Landsbank Giro, HSBC Holdings and Commerzbank were also all ranked in the top 15 underwriters of more specialized types of securities underwriting Domestic, Municipal and International Rankings, Investment Dealers Digest, January 8, 2001, at pages 43-59.

230. *See supra* text accompanying notes 14-20.

231. *See* Dibidale of La., Inc. v. Am. Bank & Trust Co., New Orleans, 916 F.2d 300, 304 (5th Cir. 1990).

232. *See* New England Co. v. Bank of Gwinnett County, 891 F. Supp. 1569, 1575 (N.D. Ga. 1995); Interchange State Bank v. Rinaldi, 696 A.2d 744, 754 (N.J. Super. Ct. App. Div. 1997).

233. *See* Pappas v. NCNB Nat'l Bank of N.C., 653 F. Supp. 699, 705 (M.D. N.C. 1987) (testimony of bank's loan officer that the bank required some of its other customers to maintain minimum balances); Gage v. First Fed. Sav. & Loan Assoc. of Hutchinson, Kan., 717 F. Supp. 745, 754 (D. Kan. 1989) (Considering testimony that the bank had never before included an option agreement such as involved in this loan.); JST Properties v. First Nat'l Bank of Glencoe, 701 F. Supp. 1443, 1450 (D. Minn. 1988) (Considering expert testimony that it was unusual as a condition of a loan to require the customer "to purchase property out of the bank's real estate portfolio.").

234. *See supra* text accompanying notes 83-87.

C. Rethinking the Bank Antitying Rules

As commercial banks begin to compete in earnest with investment banks over underwriting engagements, it will be important to analyze and rethink how the BHCA antitying provisions will affect the competition. The antitying provisions were passed in an era when commercial banks were not permitted to offer the wide extent of services and products now made possible by the GLB Act. Regardless, however, customers, the courts, banking regulators and the Department of Justice should consider how the provisions should be enforced. The GLB Act represents a huge step forward in the modernization of the capital markets of the United States, and the banking sector in particular.[235] Commercial banks can now compete on an equal footing with investment banks, opening up new markets for commercial banks to compete in. As discussed, commercial banks are particularly focused on underwriting securities at the same scale as investment banks have been doing for decades. In freeing commercial banks from their Glass-Steagall shackles, however, Congress could not have intended that commercial banks enter these markets through anticompetitive means.

The preamble to the GLB Act provides that the statute was intended "[t]o enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, insurance companies, and other financial service providers. . . ."[236] The Conference Committee Report for the GLB Act echoed the same language about enhancing competition.[237] Congress clearly intended to permit commercial banks and investment banks to compete as equals in the nation's and world's evolving capital markets.

The precursor bills and legislative history to the GLB Act also suggest that increasing competition was an important motivating factor behind the legislation. The Senate Banking Committee summarized its belief on the importance of competitive financial markets:

> The Committee believes that allowing broader affiliations within the bank holding company should place no segment of the financial services industry at a disadvantage.

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235. *See supra* text accompanying notes 57-62 (examples of new permitted activities).
236. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338, preamble (1999).
237. *See* H.R. REP. NO. 106-434 (1999). Committee of Conference, Gramm-Leach-Bliley Act.

> Banks, insurance companies, and securities firms should have equal opportunities to affiliate with one another.[238]

John D. Hawke, the Comptroller of the Currency, noted that Congress should "dismantle antiquated constraints that exist in current law" and stated that statutes should be changed to "promote increased competition."[239] The House Committee on Banking and Financial Services have emphasized the importance that legislation allow a commercial bank to "compete more effectively with other financial institutions."[240]

Unfortunately, there are no statutory provisions or legislative history that discuss how the BHCA antitying provisions should be enforced with respect to a commercial bank's exercise of these new banking powers. However, it would be inconsistent to assume that Congress would sanction a commercial bank's anticompetitive behavior as it sought to underwrite securities and exercise these new banking powers. As previously discussed, commercial banks are attempting to capitalize on the competitive advantage they enjoy by lending to their customers as well as seeking their underwriting business.

The underwriting of securities for their customers by commercial banks is becoming more commonplace. Because of this, courts will need to sort out when a commercial bank has violated the antitying provisions. The antitying provisions may be the only check left on a commercial bank's anticompetitive efforts to generate underwriting business from their borrowers. Commercial banks have already announced that few customers are profitable if the customer only looks to a commercial bank for their borrowing needs.[241] Commercial banks will be forced to further assess the overall profitability of each of their customers as they compete in even more competitive markets.

As the stakes increase in this area due to the high fees that can be earned through underwriting,[242] banking regulators and the Department of Justice should consider the importance of their role in sorting out these issues. It appears that there has been little or no direct governmental action in pursuing

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238. Financial Services Modernization Act of 1999 Report, Committee of Banking, Housing and Urban Affairs, S. REP. NO. 106-44 at 6 (1999).

239. John D. Hawke Jr., *Testimony before the Senate Banking, Housing and Urban Affairs Committee*, FEDERAL NEWS SERVICE, Feb. 24, 1999.

240. Committee on Banking and Financial Services, Committee Report on the Financial Services Act of 1999, H.R. REP. NO. 106-74, pt. 2.

241. *See supra* note 172.

242. *See supra* text accompanying notes 83-87.

violations of the BHCA antitying provisions, in spite of the power to do so.[243] All of the reported litigation in the area has been brought by private parties exercising their rights to bring a private cause of action under the statute. The threat of federal enforcement could provide a significant check against a commercial bank's unrestrained efforts to use their lending activities to generate additional underwriting engagements.

Commercial banks may cry foul if the antitying provisions are aggressively applied because investment banks are not subject to similar antitying restrictions. Investment banks are subject to the much looser tests under general antitrust law for determining whether they have tied products together. In fact, commercial banks point out that investment banks are already beginning to lend to their customers as part of the "pay to play" environment that has developed without being subject to a similar standard.[244] Such lending by the investment banks, however, has usually been at the request of the customer and is required by the customer if the investment bank wants their underwriting business. This is quite different from a commercial bank using the lending that it is already doing as a pressure point to extract additional underwriting business.

As discussed above, Congress was concerned when it passed the statutory provisions about the tremendous bargaining power enjoyed by commercial banks and was concerned that commercial banks would abuse this power by tying other products and services to the provision of credit. Given the efficiency and size of today's capital markets, it is questionable whether, in these situations, commercial banks enjoy the same monopolistic power that Congress was concerned about.

Instead of the more typical parties, privately held companies and individuals are the parties in the majority of the litigation in this area, the newly affected customers are Fortune 500 corporations or other large publicly held companies that raise money through the capital markets. These are sophisticated and large corporations that have developed extensive contacts in the capital markets and are constantly approached by commercial banks and investment banks for their business. The statute appears to assume that the commercial banks enjoy a market power with these sophisticated corporations that may not now exist to the same extent as when the statute was enacted.

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243. See *supra* text accompanying notes 145-48.
244. *See supra* text accompanying notes 122-23.

The BHCA provides ways to limit the scope and application of the antitying provisions if its application results in harsh or unjust results. The Federal Reserve is permitted to order "such exceptions to the [antitying provisions] as it considers will not be contrary to the purposes" of the BHCA.[245] Although rarely exercised in the past, such power may provide an important safety valve against liability in appropriate circumstances. The Federal Reserve should consider exercising this delegated power in order to ensure that the purpose of the antitying provisions are carried out without frustrating the purpose of GLB Act to improve competition in the U.S. capital markets.

Conclusion

The capital markets have experienced substantial structural change as commercial banks have once again regained the power to underwrite securities in open competition with investment banks. This change is being accelerated as investment banks are prodded by their customers to lend as well as underwrite securities. Unfortunately, in their drive to take advantage of these new powers to underwrite securities, commercial banks appear to be on the verge of violating the antitying provisions of the Bank Holding Company Act.

As the competition between the commercial banks and investment banks continues, the BHCA antitying provisions could prove to be an important element, to ensure that the playing field remains level. Appropriate enforcement at the federal level would ensure that commercial banks do not take advantage of their leverage as a lender as they try to persuade their large borrowers to also use them as the underwriter of their securities. Courts, however, should reassess some of the stricter interpretations of the statute in order to ensure that the antitying provisions are enforced fairly.

245. 12 U.S.C. § 1972(1) (2001).