

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

DIVISION OF CONSUMER AND COMMUNITY AFFAIRS

DATE: October 11, 2000
TO: Governor Gramlich
FROM: Beverly Smith
Phil Daher
SUBJECT: Citigroup/Associates First Capital Corporation Proposal

In light of the recently announced proposal by Citigroup, Inc. (Citigroup) to acquire Associates First Capital Corporation (AFCC), an analysis of both entity's banking subsidiaries was performed to determine the type of charter that governs their operations and to evaluate their CRA and compliance histories. As identified in the attached appendix, all of Citigroup's depository institutions were rated satisfactory or better for both CRA and compliance at their most recent examinations. Two of AFCC's banking subsidiaries also have satisfactory or better rating histories; however, one of AFCC's subsidiary bank's, Associates National Bank, received a Needs to Improve CRA rating and a "3" compliance rating at its most recent examinations.

The Associates First Capital Corporation, a Delaware corporation headquartered in Dallas, Texas, is a financial services organization that provides financing, leasing, insurance, and related services to individual consumers and businesses in the United States and internationally. AFCC operates four primary business segments, one of which is the U.S. Credit Card Segment that offers private label credit cards and VISA and Mastercard retail bankcard products distributed through three subsidiary banks, Associates National Bank, Wilmington, Delaware, Hurley State Bank, Sioux Falls, South Dakota, and Associates Capital Bank, Salt Lake City, Utah.¹ AFCC did not list any other domestic banks as subsidiaries in its December 31, 1999 SEC 10-K filing.²

All three of AFCC's subsidiary banks operate under the "nonbank" exclusions of the Bank Holding Company Act of 1956 as amended, in part, by the Competitive Equality Banking Act of 1987 (CEBA);

¹ AFCC's other business segments include: U.S. Consumer Finance Segment that offers a variety of consumer finance and insurance products, including home equity, personal, and automobile loans; Commercial Segment that provides wholesale and retail financing for heavy- and medium-duty trucks and other industrial and communications equipment; International Finance Segment that offers consumer and commercial financing products and services to consumers in Japan, Canada, United Kingdom, Puerto Rico, Sweden, Hong Kong, Spain, France, India, Mexico, Taiwan, Ireland, and Costa Rica.

² Today, the Federal Reserve Board received two notices pursuant to Regulation K for Citigroup to acquire Associates Capital Corporation, PLC, United Kingdom and Associates Financial Services (Asia), Limited, Hong Kong.

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therefore, Associates First Capital Corporation is not considered a Bank Holding Company. At this point, Board Legal indicates that Citigroup, as a Financial Holding Company, will only need to submit a post-consummation notice with the Federal Reserve Bank of New York, and not file an application under the BHC Act. Consequently, there will be no formal comment period for this acquisition. Staff notes, however, that Citigroup would be required to file Change in Bank Control Notices with the OCC and the FDIC prior to acquiring AFCC's depository subsidiaries.³

Under the Gramm Leach Bliley Act (GLBA), bank holding companies with a subsidiary rated less than satisfactory for CRA are not precluded from becoming an FHC if the entity in question were acquired within the previous 12 months and if management has provided the primary regulator with a CRA plan to address the deficiencies. However, GLBA and the interim regulation do not address situations in which an existing FHC proposes to acquire an institution with a less than satisfactory CRA rating. This issue is currently under review in the context of drafting the final regulation.

Associates National Bank

The Associates National Bank (ANB) is an OCC regulated CEBA bank that is only permitted to engage in credit card lending. At ANB's most recent Consumer Compliance and CRA examinations conducted on March 30, 1997, the bank received a "3" compliance rating and a Needs to Improve CRA rating.⁴ The less than satisfactory ratings were caused by significant violations of Regulation B that were referred to the Department of Justice. OCC examiners cited ANB for the disparate treatment of applicants and cardholders who utilized Spanish-language applications when applying for ANB's UNOCAL 76 Mastercard and ANB Hispanic credit card products. Examiners found no evidence of illegal disparate treatment in ANB's other credit card products. ANB was scheduled for follow-up Compliance and CRA examinations in the first quarter of 1999; however, in its October 25, 1999 Safety and Soundness report of examination, the OCC noted that the examinations have been postponed until the current fair lending violations and the DOJ referral have been resolved.

³ Citigroup has filed CIBC notices with both the OCC and the FDIC and both agencies have extended the public comment period by two weeks to October 18, 2000. The OCC has publicly stated that it will not be holding public hearings; however, while the FDIC has indicated that they do not intend to hold public meetings, a public announcement has not been made.

⁴ Previous Consumer Compliance and CRA examinations conducted on April 24, 1995 resulted in ANB receiving a "2" compliance rating and a composite "22222/2" CRA rating under the "old" regulation. ANB also was examined for compliance with CRA on March 8, 1993 and received a "33223/3" rating. The overall "3" rating was caused by the limited lending, investment, and community development activities allowed by ANB's CEBA charter. The bank was rated satisfactory under the performance categories of Geographic Distribution and Discrimination and Other Illegal Credit Practices.

Examiners found that ANB had improperly declined or assigned lower credit limits to applicants who utilized Spanish-language credit card applications. In addition, cardholders who applied through Spanish-language applications were excluded from certain programs offered to other cardholders. Examiners noted that the violations were caused by changes made in the bank's credit processing decision trees and credit limit assignment matrices. Changes were made in ANB's English-language application underwriting processes without similar adjustments to the corresponding Spanish-language application underwriting mechanisms, resulting in different programs and possibly less favorable terms being provided to cardholders who had applied through Spanish-language applications. ANB management stated that the modifications were made to address volume decreases in its credit card portfolio, and since a large volume of credit card activity reportedly came from English-language applications, the Spanish-language decision trees and credit limit assignment matrices were overlooked and not changed.⁵ Management further stated that cardholders within smaller or specialized portfolios (including accounts generated from Spanish-language applications) were excluded from certain promotional offers because of their very small size and the need to customize marketing materials in the Spanish language.

OCC examiners also identified instances of disparate treatment in the assignment of credit limits where standard UNOCAL 76 applicants received higher credit limits than applicants with the same qualifications who used Spanish-language applications. The account holders included Spanish-language applicants in a FICO score range which had not been previously identified as being affected by ANB's use of different credit limit assignment matrices. ANB management agreed that their corrective actions should be expanded to include cardholders within this identified FICO score range.

ANB management ceased the identified discriminatory practices on April 21, 1997 and applications for all credit cards are now processed through the same decision tree with Spanish- and English-language applications receiving equal treatment. Furthermore, cardholders who had applied through Spanish-language applications are now included in all credit card programs. Bank management identified applicants who may have been improperly denied credit or who were approved but potentially given lower credit limits and the bank re-offered products and increased credit limits where warranted. To address cardholders who lost opportunities for more favorable credit terms, ANB offered a special balance consolidation product exclusively to these cardholders. Management also strengthened its fair

⁵ Examiners contacted Maryanne Kennedy of the OCC who was the Examiner-in-Charge during the examination where the discriminatory practices were identified. She clarified the examination report adding that ANB had loosened its underwriting standards in its English-language credit card application underwriting decision trees in order to address an overall decrease in credit card volume without making similar adjustments in the Spanish-language credit card application underwriting systems.

lending compliance program to include second reviews of all decision tree changes and marketing programs.

Hurley State Bank

Hurley State Bank (HSB) is an FDIC regulated CEBA bank that was acquired by First Capital Corporation in October 1998. HSB offers only private label credit card products and is a limited purpose institution under CRA. The bank was examined for Consumer Compliance and CRA by the FDIC on April 19, 1999 and received a "1" rating for compliance and a Satisfactory rating under the CRA limited purpose bank guidelines. In its Consumer Compliance report of examination, the FDIC noted that HSB's compliance management program is heavily influenced by its affiliate, Associates National Bank.

Associates Capital Bank

The Associates Capital Bank (ACB) is an FDIC regulated Industrial Loan Company chartered by the state of Utah that offers consumer and commercial credit card products and real estate loans across the nation.⁶ At its most recent Consumer Compliance and CRA examinations conducted by the FDIC on September 27, 1999, ACB received a "1" compliance rating and an Outstanding CRA rating. Previous examination reports from 1996 and 1994 also noted that the bank had a strong compliance program and a satisfactory record of CRA performance.⁷

Other Fair Lending Issues

The DOJ is currently investigating a number of subprime lenders, including AFCC, with respect to possible violations of the anti-discrimination laws. In addition, the FTC has an ongoing two-year investigation of AFCC with respect to predatory lending and violations of the Unfair and Deceptive Credit Practices Act, and a draft complaint and proposed Consent Order has been forwarded to AFCC by the FTC. Staff at the FTC are awaiting a response from AFCC before pursuing the matter in court.

⁶ Prior to February 14, 1998, Associates Capital Bank operated under the names Associates Investment Corporation and Associates Financial Services Company of Roy, Inc.

CC: Dolores Smith
Glenn Loney
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Summary Ratings ChartsCitigroup, Inc.

D.I. Name (RSSD #)	Regulator	CRA Rating (Date)	Compliance Rating (Date)
Citibank, N.A. New York City, New York (#476810)	OCC	Satisfactory (1/10/00)	2 (1/10/00)
Citibank N.A. Las Vegas, Nevada (#455365)	OCC	Outstanding (3/29/99)	1 (3/29/99)
Citibank Pittsford, New York (#536219)	FDIC	Satisfactory (3/6/00)	112/1 (3/6/00)
Citibank, N.A. Sioux Falls, South Dakota (#486752)	OCC	Outstanding (5/24/99)	1 (5/24/99)
Citibank New Castle, Delaware (#490115)	FDIC	Outstanding (5/15/00)	111/1 (5/15/00)
Citicorp Trust, N.A. Palm Beach, Florida (#449038)	OCC	Exempt	Exempt
Citibank, FSB San Francisco, California (#2132660)	OTS	Outstanding (7/12/99)	1 (7/12/99)
Citicorp Trust, N.A. Los Angeles, California (#596361)	OCC	Exempt	Exempt
Universal Bank, N.A. Columbus, Georgia (#1442380)	OCC	Satisfactory (2/22/99)	1 (10/5/98)
Universal Financial Corp. Salt Lake City, Utah (#193470)	FDIC	Satisfactory (3/31/99)	111/1 (3/31/99)
Travelers Bank & Trust Newark, Delaware (#374112)	OTS	Satisfactory (11/30/98)	Satisfactory (11/1/98)
Citibank USA Newark, Delaware (#1404931)	FDIC	Outstanding (3/15/99)	111/1 (3/15/99)

Associates Capital Corporation

D.I. Name (RSSD #)	Regulator	CRA Rating (Date)	Compliance Rating (Date)
Associates National Bank Newark, Delaware (# 1833063)	OCC	Needs to Improve (3/30/97)	3 (3/30/97)
Hurley State Bank Sioux Falls, South Dakota (#112855)	FDIC	Satisfactory (4/19/99)	1 (4/19/99)
Associates Capital Bank Salt Lake City, Utah (#2035716)	FDIC	Outstanding (9/27/99)	1 (9/27/99)