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December 21, 2007

**By Hand Delivery**

Regulation Comments  
Chief Counsel's Office  
Office of Thrift Supervision  
1700 G St., N.W.  
Washington, D.C. 20552

Re: Docket ID OTS-2007-0008

Ladies and Gentlemen:

This comment letter is in response to the interim final rule regarding prohibited service at savings and loan holding companies ("Interim Rule") published by the Office of Thrift Supervision ("OTS") on May 8, 2007.<sup>1</sup> We represent a large, diversified corporation that owns a federal savings bank. As a savings and loan holding company ("SLHC"), our client is subject to section 19(e) of the Federal Deposit Insurance Act ("Section 19") and the new Part 585 of the OTS regulations. We appreciate this opportunity to comment on the Interim Rule.

**Background**

For many years, our client has had in place as part of its standard hiring program a process for screening prospective employees consisting of criminal history questions on its employment application (inquiring about all felony convictions, and misdemeanor convictions occurring during the prior seven years, as allowed by law), the responses to which are then confirmed by an independent background check. In response to the Interim Rule, our client devoted significant resources to the development of a process for screening its extensive employee base regarding all felony or misdemeanor convictions and pretrial diversion program entries for offenses involving dishonesty or breach of trust, regardless of the time elapsed since any such offense.<sup>2</sup> The process involved the development of a custom technology tool to distribute the appropriate questions to its employees, track responses, and generate reminders.

<sup>1</sup> Prohibited Service at Savings and Loan Holding Companies, 72 Fed. Reg. 25948 (May 8, 2007) (to be codified at 12 C.F.R. pt. 585).

<sup>2</sup> Our client initiated a Section 19 screening process in anticipation of the September 5, 2007 expiration of the temporary exemption under section 585.100(b) and completed its initial screen of all employees in advance of the OTS's extension of this exemption until March 1, 2008.

This extensive process yielded positive responses for offenses that may possibly require an exemption request to the OTS at a rate of approximately one-tenth of one percent of the population screened. More importantly, the offenses picked up by the expanded scope of the Interim Rule are predominantly minor in nature, primarily older misdemeanors and pretrial diversion program entries. While this yield was in line with our client's expectations—based in large part on the new hire vetting process in place before the Interim Rule—it was a noticeably low return for the resources invested. In developing this Section 19 screening process and fielding employee questions and responses, our client gained valuable insight into the practical implications of the Interim Rule, which may be of interest to the OTS.

### Discussion

As a result of our client's recent experience in screening a large employee population in accordance with the Interim Rule, we offer the following suggested revisions to the Interim Rule:

- Most importantly, the scope of SLHC employees subject to the Interim Rule should be those employees who are in positions where they could potentially impact an SLHC, specifically, an SLHC's major policymakers.
- An automatic temporary exemption should be granted for employees inherited by SLHCs pursuant to acquisitions to allow SLHCs time to screen such employees.
- The relationship between the Interim Rule and applicable state, federal, and foreign laws should be clarified.
- The exemption for *de minimis* offenses should be revised to: (i) clarify that the "only offense" requirement pertains only to Section 19-covered offenses; (ii) define a *de minimis* offense by reference to the actual penalty imposed, where available, rather than the statutory maximum; (iii) for offenses measured by maximum penalty, extend the exemption to offenses for which the maximum penalty could be up to a year in prison; and (iv) increase the maximum fine amount to \$5,000 to account for higher misdemeanor penalties.
- Older pretrial diversion programs should be exempt from coverage.

Each of these suggestions is discussed in more detail below.

I. Application of Section 19.

A. *Scope of Covered Population*

As currently written, the Interim Rule covers a significant population of our client's employees. Most of the employees included in the covered population have no working relationship with the federal savings bank and do not hold positions that would enable them to impact policy at the SLHC, including administrative assistants, lab technicians, and maintenance workers, among others. They are covered by the Interim Rule simply because their responsibilities and activities are not limited solely to those exempt under section 585.100(a)(1). In actuality, these employees have no greater ability to affect the SLHC or its subsidiary federal savings bank as employees of the SLHC than they would as employees of a non-depository institution subsidiary of the SLHC or employees engaged in exempt activities.

While our client's interests and those of the OTS are aligned with respect to the importance of not employing persons who may pose a risk to the SLHC or its subsidiary federal savings bank, we believe that this objective may be accomplished with a more narrow scope. As currently drafted, there is little correlation between the minimal risk posed to SLHCs and the broad scope of the Interim Rule. While an attempt could be made to broaden the list of exempt activities in section 585.100(a)(1) to encompass more support personnel, it is impossible to contemplate all activities in which SLHC employees may engage in the future (*e.g.*, healthcare, education, hospitality management).

Instead, we suggest that the scope of the Section 19 covered population be narrowed to encompass solely those employees who truly have the ability to impact an SLHC or its subsidiary insured depository institution, particularly with respect to policymaking. Because our client and many SLHCs have existing screening and hiring practices, exempting non-policymaking employees from Part 585 would not pose a material risk to SLHCs. Accordingly, we recommend limiting the scope of the Interim Rule to the directors and major policymakers of an SLHC. Each SLHC could maintain a list of its major policymakers subject to Section 19. The Interim Rule already contemplates such a list for other purposes. SLHCs could make their lists available for their examiners to review. This approach would direct an SLHC's resources to the positions that pose the most significant risk, and would be not unlike the approach taken with respect to the prohibitions against loans to insiders in Regulation O of the Board of Governors of the Federal Reserve System.

B. *Treatment of Acquired Employees*

As the OTS is aware, many SLHCs are diversified companies engaged in a variety of business activities not related to their subsidiary insured depository institutions. Our client and other SLHCs often expand their businesses through acquisitions. In a standard acquisition, our

client has no opportunity to screen prospective employees in advance of acquiring them on the closing date. Prior to closing, the prospective employees are employees of the seller, thus our client is not permitted to screen them. In addition, the seller typically lacks standing to screen the employees, as the targets of acquisitions generally are not subject to Section 19. In most cases, the acquired employees immediately become employees of the SLHC as of the closing date and, to the extent that any acquired employees have a covered offense in their history, the SLHC is afforded no opportunity to seek exemptions in appropriate cases.

Accordingly, we propose that the OTS grant an automatic temporary exemption from the application of Section 19 for such newly acquired employees to permit SLHCs to properly screen the employees and file exemption requests as necessary. The exemption should run from the closing date of the acquisition, and should provide sufficient time to permit an SLHC to fully vet the newly hired employees (possibly 90 days). Such a temporary exemption would be similar to the exemption granted to existing SLHC employees under section 585.100(b).

## II. Conflicts of Laws.

### A. *U.S. State and Federal Laws*

Many state laws expressly prohibit criminal history inquiries other than with respect to convictions (*e.g.*, pretrial diversion program entries), and also specifically limit the permissible retrospective period (*e.g.*, inquiries beyond seven years are prohibited). Where an SLHC such as our client exceeds the state law boundaries with respect to individuals who are in fact subject to Section 19, the SLHC may argue that application of the state laws is preempted by Section 19. However, to the extent that the SLHC, out of an abundance of caution, screens employees or potential employees whose coverage by Section 19 is subject to interpretation, the SLHC may be pressed to defend its classification of the actual or potential employee as covered by Section 19 and its questioning of that employee.

SLHCs' efforts to comply with the broad reach of the Interim Rule as currently drafted also may expose them to potential civil suits and enforcement actions under federal and state anti-discrimination statutes. The Equal Employment Opportunity Commission ("EEOC"), which enforces the anti-discrimination provisions of Title VII of the Civil Rights Act of 1964, has taken the position (which is supported by empirical data) that the consideration of criminal history in making employment decisions adversely impacts minority job candidates. Such disparate impact gives rise to liability unless the employer can show that the criminal history considered is job-related or that the employer has some other articulable "business necessity" justifying any adverse employment action based on criminal history. In examining employers' actions in this area, the enforcement agencies also consider the severity and age of the crime. It is more difficult for an employer to justify its consideration of older, less severe offenses than more recent, more severe crimes. Moreover, SLHCs are likely to face more challenges on

employment law grounds than their insured depository institution subsidiaries, as the connection between the safety and soundness of an insured depository institution and offenses (especially older, more minor offenses) committed by non-policymaking employees at the holding company level is not readily apparent.

To address these risks, we reiterate our request that the OTS narrow the scope of the population subject to Section 19, as discussed in Section I above. We propose that the population should be clearly and appropriately defined, with consideration given to risks arising under federal and state employment laws. In addition, we suggest that the OTS revise the Interim Rule to clearly state that Section 19 and Part 585 preempt state laws to the extent there is a conflict. We propose that the OTS frame the preemption language broadly enough to create a safe harbor for SLHCs to the extent that, in a good faith effort to comply with Section 19 and Part 585, SLHCs incorrectly classify an employee as subject to Section 19 and make a criminal history inquiry that is impermissible under state law.

#### B. *Foreign Jurisdiction Laws*

Many SLHCs, including our client, employ people in foreign jurisdictions. Many foreign jurisdictions have strict privacy and employment laws which, among other things, restrict an SLHC's ability to inquire about potential and actual employees' criminal histories, limit the SLHC's ability to share any criminal history information with the OTS, or prohibit the SLHC from taking any adverse action against the individual (e.g., not extending an employment offer, terminating an existing employee, or even moving an employee from a Section 19 covered position to a non-covered position) as a result of any criminal history information. In those jurisdictions, an SLHC's efforts to comply with the Interim Rule would require the SLHC to violate the law of a sovereign nation.

Again, our request to limit the scope of the Section 19 covered population to an SLHC's major policymakers would alleviate some of the risk associated with applying Section 19 in foreign jurisdictions. In addition, we propose that the OTS clarify the Interim Rule to state that nothing in Part 585 requires SLHCs to violate foreign law. In such jurisdictions, we propose that the OTS require SLHCs to comply with Section 19 and Part 585 to the extent permitted under local laws, based on the SLHC's analysis of such local laws. The OTS could require SLHCs to screen employees in the event they move from a jurisdiction where screening is impermissible to a jurisdiction where screening is permissible.

#### III. *De Minimis Rule.*

The Interim Rule currently grants a blanket exemption for offenses deemed to be *de minimis* in that they are of such a minimal nature as to pose little, if any, risk to an SLHC or its subsidiary insured depository institution. In part, an employee qualifies for the *de minimis*

exemption if (i) the employee has “only one conviction or pretrial diversion or similar program of record” and (ii) the offense is punishable by “imprisonment for a term of less than one year, a fine of less than \$1,000, or both” and the person did not serve any jail time.<sup>3</sup>

A. *Only Conviction*

Unlike the FDIC’s Statement of Policy regarding Section 19 (“FDIC Policy Statement”),<sup>4</sup> the Interim Rule is not entirely clear as to whether the single conviction prong of the *de minimis* exemption requires that the current offense is the individual’s only conviction or pretrial diversion for an offense covered by Section 19, or the individual’s only conviction or pretrial diversion for any type of offense, whether or not covered by Section 19. If, in order to qualify for the *de minimis* exemption, an SLHC must ask potential and current employees about offenses not covered by Section 19, the SLHC may be in violation of state or federal employment laws. By contrast, the FDIC Policy Statement requires that, to qualify for the *de minimis* exemption, the current offense is the individual’s only conviction or pretrial diversion for a covered offense.<sup>5</sup> We propose that the OTS adopt the same approach as the FDIC and revise the *de minimis* exemption to clarify that the current offense must be the individual’s only conviction or program entry for offenses covered by Section 19.

B. *Actual Penalty*

As mentioned above, the exemption for *de minimis* offenses is designed to identify those offenses which are of such a minor nature as to pose little risk to SLHCs and their subsidiary insured depository institutions. Statutory penalties are, by necessity, broadly drawn. By contrast, the actual penalty imposed reflects the determination made by a judge or jury as to the appropriate penalty for the crime committed, which is a better proxy for the risk posed by an individual’s criminal history.

For these reasons, we propose that the OTS revise the *de minimis* test to reference, where available, the actual penalty imposed for convictions and any specific sentence deferred in pretrial diversion program entries. Where specific sentencing information is unavailable, reference to the statutory maximum penalty would be an appropriate alternative.<sup>6</sup>

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<sup>3</sup> 72 Fed. Reg. at 25956 (12 C.F.R. § 585.50(b)(1)–(2)).

<sup>4</sup> Statement of Policy Pursuant to Section 19, 63 Fed. Reg. 66177 (Dec. 1, 1998).

<sup>5</sup> *Id.* at 66185.

<sup>6</sup> The *de minimis* test also requires that the individual did not serve any time in jail in connection with the offense at issue. We are not suggesting that this aspect of the test be revised or eliminated. Under our proposal, the maximum term of imprisonment would only apply in instances where the actual penalty (*i.e.*, the amount of the fine imposed) is not available.

C. *Maximum Term of Imprisonment*

The *de minimis* test in the Interim Rule also requires that the offense in question be punishable by less than one year of imprisonment, a fine of less than \$1,000, or both. However, it has been our client's experience that state statutes for minor, misdemeanor offenses often impose maximum penalties of "up to" (and including) a year in prison and/or a \$1,000 fine.<sup>7</sup> In addition, federal law provides that the lowest level of felony offense is punishable by *more than* one year in prison.<sup>8</sup> Thus, many old, otherwise *de minimis* offenses for which the actual penalty imposed was typically a small fine, would not qualify for the *de minimis* exemption because they carry maximum penalties that are one day and \$1 more than those contemplated by the Interim Rule.

We propose the OTS expand the scope of this prong of the *de minimis* test to encompass crimes for which the maximum penalty is up to one year in prison. Increasing the maximum penalty, even by one day, will likely exempt a significant number of additional minor offenses which pose little risk to SLHCs and their subsidiary insured depository institutions, and for which filing exemption requests would be an inefficient use of SLHC and OTS resources. As we have already noted, including offenses punishable by a maximum of one year in prison would be consistent with the demarcation used in many state statutes and federal law. Moreover, such an approach would be consistent with the companion statute to Section 19 at 12 U.S.C. § 1818(g), which permits the suspension or removal of an institution affiliated party charged with a crime involving dishonesty or a breach of trust "which is punishable by imprisonment for a term exceeding one year." In addition, the OTS has recognized the merit of distinguishing offenses punishable by more than one year in prison. The OTS optional bylaw regarding director integrity similarly refers to offenses involving dishonesty or breach of trust for which the penalty may be "imprisonment for more than one year."<sup>9</sup>

D. *Maximum Fine*

Our client has found that some misdemeanor offenses are punishable by fines exceeding \$1,000, often up to \$5,000.<sup>10</sup> Thus, while expanding the *de minimis* test as outlined above would pick up certain additional minor offenses, it would continue to exclude other misdemeanor offenses that are *de minimis* in fact, such as possession of stolen property under Indiana law.<sup>11</sup>

<sup>7</sup> See, e.g., Cal. Penal Code §§ 148.3, 483.5; N.Y. Penal Law §§ 165.40 (possession of stolen property is a class A misdemeanor), 70.15(1), 80.05(1) (class A misdemeanor maximum penalty).

<sup>8</sup> 18 U.S.C. § 3559.

<sup>9</sup> OTS, Applications Handbook sec. 410.33.

<sup>10</sup> Ind. Code § 35-50-3-2 (class A misdemeanor punishable by up to one year in prison and a fine of \$5,000). See also Tex. Penal Code Ann. § 12.21-23 (Providing that class A and B misdemeanors are punishable by fines of up to \$4,000 and \$2,000, respectively. Only class C misdemeanors, punishable by fines up to \$500, would satisfy the current *de minimis* test.).

<sup>11</sup> *Id.* §§ 35-43-4-3, 35-50-3-2.

We suggest that the OTS increase the maximum fine prong of the *de minimis* test to accommodate these additional offenses. As with the maximum term of imprisonment, this revision would exempt additional minor offenses which pose little risk and for which filing exemption requests would be an inefficient use of SLHC and OTS resources.

#### IV. Pretrial Diversions.

In addition to convictions for offenses involving dishonesty or a breach of trust, the Interim Rule also applies to any agreement by an individual to enter into a pretrial diversion program in connection with the prosecution for such an offense. In discussing the inclusion of pretrial diversion programs in the scope of Section 19, the FDIC Policy Statement notes the minor nature of offenses typically qualifying for pretrial diversion programs and the limited risk posed to financial institutions from older pretrial diversion program entries.<sup>12</sup> Accordingly, the FDIC Policy Statement grants an exemption for all pretrial diversion program entries occurring prior to November 29, 1990, the effective date of the extension of Section 19 to pretrial diversions.<sup>13</sup> The OTS similarly acknowledges the minor nature of most offenses eligible for pretrial diversion programs, but the Interim Rule does not include a similar exemption for older pretrial diversion program entries. The lack of such an exemption is incongruous with the risk-based balance that the Interim Rule otherwise attempts to achieve, as evidenced by the exemption afforded *de minimis* offenses and employees engaged in exempt activities. Moreover, the lack of such an exemption creates an inconsistent regulatory environment where the Section 19 standard at the SLHC level is more stringent than the standard applicable to insured depository institutions.

Our client has found it challenging to obtain documents and confirm details regarding pretrial diversion program entries occurring more than a few years ago. It is our understanding that courts often remotely store or destroy records regarding minor offenses after a few years and individuals typically do not retain such records, justifiably believing that they are unlikely to need to produce such records in the future. In light of the minimal nature of offenses typically eligible for pretrial diversion programs, the negligible risk posed to SLHCs and their subsidiary insured depository institutions as a result of such offenses, and the difficulty for SLHCs to acquire documentation and confirm the details and adjudication of such offenses, we believe it would be appropriate for the OTS to recognize some form of exemption for older pretrial diversion programs. Such an exemption would also be consistent with applicable state, federal, and foreign laws prohibiting inquiries regarding older crimes. We suggest that the OTS acknowledge the inverse relationship between the age of a pretrial diversion program entry and the risk posed to the SLHC, by exempting all pretrial diversion program entries occurring a defined period of time (*e.g.*, seven or ten years) prior to the later of (i) the effective date of a final

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<sup>12</sup> 63 Fed. Reg. at 66180.

<sup>13</sup> *Id.*

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rule regarding Section 19 issued by the OTS, or (ii) the date on which the individual first holds his or her current Section 19-covered position. Alternatively, we recommend an exemption for all pretrial diversion program entries occurring prior to November 29, 1990, the effective date of the extension of Section 19 to pretrial diversion program entries, which is consistent with the FDIC approach.

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We trust that the foregoing is useful in evaluating the effects of the Interim Rule. We propose that the changes suggested herein would strike the appropriate balance between mitigating risks posed to SLHCs and conserving SLHC and OTS resources.

If you have any questions regarding this matter, please call me at (202) 736-8267.

Sincerely,



William S. Eckland

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