FMWATCH

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March 31, 2000

BY HAND DELIVERY

Secretary Donald Clark
Federal Trade Commission
Room H-159
600 Pennsylvania Avenue, NW
Washington, DC 20580

Re: Gramm-Leach-Bliley Act Privacy Rule, 16 CFR Part 313 – Comment

Exclusion of Government Sponsored Enterprises from the Definition of Financial Institution, Section 313.3(j)(3)(iii)

Dear Mr. Clark:

We are writing to comment on the Federal Trade Commission's ("FTC") proposed rule, Section 313.3(j)(3)(iii), implementing Section 509(3)(D) of the Gramm-Leach-Bliley Act, Pub. L. No. 106-102 ("GLB Act" or "Act"). As explained below, the proposed rule does not adequately limit the use of nonpublic personal information by institutions chartered by Congress to engage in securitizations and secondary market sales.

Provisions of the GLB Act

Congress enacted Title V of the GLB Act to implement its policy that each financial institution has an affirmative and continuing obligation to respect the privacy of its customers. GLB Act, § 501(a). The Act requires financial institutions to provide their customers with notice of the institution's practices regarding disclosure of nonpublic personal information and to give consumers with whom they do not have an ongoing relationship notice if they would be disclosing information about that consumer. Congress also prohibited the disclosure of nonpublic personal information to certain nonaffiliated third parties unless the consumer was given notice that such information would be shared, was given the opportunity to opt out of such disclosure, and chose not to opt out. *See* GLB Act, § 502(a). One of the situations in which information can be shared with nonaffiliated third parties is "a proposed or actual securitization, secondary market sale (including sales of servicing rights), or similar transaction related to a transaction of the consumer." GLB Act, § 502(e)(1)(C).

In addition to the exclusion for information disclosed in connection with secondary market transactions, institutions chartered by Congress to engage in securitizations and secondary market transactions, also known as government sponsored enterprises ("GSEs"), are excluded from the Act's definition of "financial institution" as long as they do not sell or transfer information to a nonaffiliated third party. GLB Act, § 509(3)(D).

As the Conference Report explains, "[t]he Conferees granted the exception based on the understanding that the covered entities do not market products directly to consumers." Conference Report 106-434, 106th Cong., 1st Sess., Nov. 2, 1999, p. 172.

FTC Proposed Regulation

Proposed section 313.3(j)(3)(iii) provides:

> Financial institution does not include . . . (iii) Institutions chartered by Congress specifically to engage in securitizations, secondary market sales (including sales of servicing rights) or similar transactions related to a transaction of a consumer, as long as such institutions do not sell or transfer nonpublic personal information to a nonaffiliated third party other than as permitted by §§ 313.10 and 313.11 of this part.

In implementing section 509(3)(D), the FTC interprets the statutory language broadly, excluding GSEs from the definition of financial institution and the accompanying responsibilities and limitations not only when using information for secondary market activities, but also when selling and transferring consumer data to certain nonaffiliated third parties in direct contradiction to the language of the Act. As the FTC explains in the Section-by-Section analysis, it interprets the Act's exception for the GSEs to apply even if the chartered institutions sell or transfer information to a third party to whom disclosure is permitted under section 502(e).

This broad interpretation contravenes the language and spirit of the Act. The statute excludes the GSEs from "financial institution" by referring back to the excluded activities, which are limited to securitizations, secondary market sales, or similar transactions. FM Watch believes that the reference in section 509(3)(D) to section 502(e)(1)(C) operates to confine the GSEs' exemption from the definition of financial institution. The Conference Report indicates a congressional intent to limit the use of information by congressionally chartered institutions. The GSEs were chartered by Congress to accomplish specific purposes: to provide stability and liquidity in the secondary market for residential mortgages and to promote access to mortgage credit. These goals do not require the GSEs to use information for any purpose unrelated to the secondary market.

The FTC's proposed rule fails to limit the GSEs' use of information under the exmeption to the purposes indicated in the Conference Report. Furthermore, the proposed rule expands the exception to permit the GSEs to sell or transfer information despite the language of section 509(3)(D) of the Act, which provides that the GSEs lose their exclusion if they sell or transfer nonpublic personal information to a nonaffiliated third party, making them subject to the same limitations and obligations as other financial institutions. The FTC's proposed interpretation would allow the GSEs to share consumer data for purposes unrelated to their secondary market mission without disclosing their

privacy policies to the consumers whose data were being shared. Based on the language of the statute and the accompanying Conference Report, we believe that this goes beyond Congressional intent.

The interpretation proposed by the FTC does not limit the GSEs from contracting with a third party for the GSEs to provide services or products offered by that third party to consumers. The institutions chartered by Congress are given a special position in the mortgage market. As the primary pipeline for conventional mortgage loans to be sold into the secondary market, the GSEs receive nonpublic personal information about consumers and their properties for 74% of the conventional mortgage market.[1] The GSEs have substantial databases from all of the loans they have purchased that will enable them to data-mine the information to target consumers for certain products or services. They could market any financial product or service from a third party directly to consumers for a fee without having to sell or transfer the information. While private entities may have similar marketing opportunities, they do not enjoy an exclusion from Title V of the GLB Act. Private entities have not received federal subsidies that allow them to create immense databases nor have they been granted a special position in the mortgage market by the federal government that ensures information on a huge number of consumers is being fed into their databases.

The GLB Act recognized the need to disclose nonpublic personal information to enable the securitization and secondary market sale of mortgages. Permitting the GSEs' use of information for purposes outside of this prescribed use violates the purpose of the GLB Act.

Suggested Revisions

The FTC is given regulatory authority in Section 504 to carry out the Act's purposes. To meet the purpose of Title V in protecting consumers' privacy and to give effect to the position stated in the Conference Report, the FTC should adopt a regulatory provision that limits the GSEs' use of nonpublic personal information to the institutions' activities in the secondary market. We recommend that Section 313.3(j)(3)(iii) be revised as follows:

> Financial institution does not include . . . (iii) Institutions chartered by Congress specifically to engage in securitizations, secondary market sales (including sales of servicing rights) or similar transactions related to a transaction of a consumer, as long as the institution
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> (a) does not sell or transfer nonpublic personal information to a nonaffiliated third party ; and

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1 Peter J. Wallison and Bert Ely, "Nationalizing Mortgage Risk: The Growth of Fannie Mae and Freddie Mac," American Enterprise Institute, March 2000.

(b) does not use a consumer's nonpublic personal information for any purpose unrelated to securitizations, secondary market sales (including sales of servicing rights) or similar transactions related to a transaction of a consumer.

This revision would allow the secondary market to function efficiently while giving consumers the protections promised by the Act. This revision would not prohibit the GSEs from sharing information. Under this revision, should a GSE use a consumer's nonpublic personal information for reasons unrelated to its secondary market role, it would simply lose (with respect to such data sharing) its special exemption from the definition of "financial institution." Thus, such data sharing would be permitted, prohibited or regulated in exactly the same way as it would be if it were undertaken by any other financial institution. In addition to providing consumers with the privacy protections they are meant to be afforded by the Act, the revision would help to create a more level playing field when the GSEs compete with fully private institutions in market areas other than those for which Congress chartered the GSEs.

If you have any questions, please contact me at 202-637-5636, or Pamela Blumenthal at 202-637-5561.

Sincerely,

Mike House
Executive Director