
2004 CREDIT ACCESS SURVEY

*Linking Corporate Credit to the Awarding
Of Other Financial Services*

Report of Survey Results

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7315 Wisconsin Avenue, Suite 600 West, Bethesda, MD 20814
301.907.2862 Fax 301.907.2864 www.AFPonline.org

Executive Summary

Financial professionals continue to report that commercial banks frequently make access to credit contingent upon the purchase of other financial services, despite assertions by regulatory bodies to the contrary. Large companies—those with annual revenues greater than \$1 billion—are more likely to be subject to banks' attempts to link credit access to other financial services. Large companies are more likely to be subject to linking activity, in part because their size and complex credit needs limit the number of commercial banks that are able and willing to serve them. Many respondents indicate that the pressure to award other business continues to increase because there are fewer alternate banks that are able and willing to meet their credit needs as a result of commercial bank consolidation.

Section 106 of the Bank Holding Company Act (BHCA) prohibits commercial banks from linking corporate credit to the purchase of some additional product or service from the bank or its affiliate. While certain products and services are exempt from the BHCA, either by statute or regulation, there is ambiguity as to the products and services that can and cannot be linked to corporate credit. While regulators have indicated that there is no widespread illegal activity, financial professionals have reported in previous surveys conducted by the Association for Financial Professionals (AFP) that commercial bank credit providers denied credit or changed the terms of credit after their company did not award other financial business.

In February 2004, AFP conducted its third survey on this subject. Among the key survey findings:

- Nearly two-thirds of financial professionals from large companies report that their commercial bank credit providers denied credit or changed the terms of credit after the company did not award other financial business.
- Financial professionals indicate that their company has been subject to activity that the Federal Reserve Board has stated to be illegal:
 - One out of seven large companies report that in the past five years they have been explicitly required by a commercial bank to obtain corporate debt and/or equity underwriting services from an affiliate of the bank in order to obtain a loan from the bank.
 - Half of large companies are unable to meet revenue targets imposed by a commercial bank without awarding bond or equity underwriting and/or strategic advisory services.
 - More than a quarter of respondents from large companies indicate that they have been subject to exclusive dealing requirements from a commercial bank.

- Most companies indicate that they are under pressure from their credit providers to award other business.
 - Ninety-six percent of respondents from large companies report that their company is subject to pressure from their credit providers to award other business.
 - Nearly half of large companies report that this pressure to award additional business has been increasing over the last year.
- Financial professionals report that their company has fewer options for commercial credit, due to commercial bank consolidation.
 - Nearly three out of five respondents from large companies report that the number of banks that are willing and able to meet their company's credit needs has decreased over the past five years.
 - Many financial professionals believe the continuing consolidation of commercial banks will lead to decreased credit availability, higher priced bank credit, higher prices for cash management services and greater negotiating power for commercial banks.

For the third time in three years, financial professionals—especially those from large companies—report that their companies have been denied credit or had credit terms changed by a commercial bank because the company did not award other financial business. A significant number of survey respondents note that their company has been subject to activities that the Federal Reserve indicates would violate Section 106 of the Bank Holding Company Act. Further, many companies continue to report that the pressure to award business has increased over the past year. Financial professionals also are concerned that, as a result of consolidation among large commercial banks, their companies have fewer banks that are willing and able to meet their company's credit needs.

Background

In response to the large number of bank failures during the Great Depression, Congress passed the Banking Act of 1933. The part of the law known as the Glass-Steagall Act restricted commercial banks from dealing in and holding corporate securities. This was modified when Congress passed the Bank Holding Company Act Amendments of 1970 (BHCA). Section 106 of the BHCA prohibits banks from extending credit or furnishing any product or service, or varying the price of any product or service, on the “condition or requirement” that the customer obtain some additional product or service from the bank or its affiliate. This activity is commonly referred to as “tying.” Some tying arrangements are specifically exempted from the BHCA, either by statute or regulation. However, there is a lot of ambiguity as to the products and services that can and cannot be “tied.”

In 1999, Congress passed the Gramm-Leach-Bliley Act (GLB), which repealed restrictions on commercial banks that prohibited them from dealing in and holding corporate securities. With the enactment of GLB, commercial banks could combine with investment banks and insurance companies to form financial holding companies. Banking organizations could again sell their corporate clients both credit and investment banking services. However, GLB did not repeal the anti-tying prohibitions of the BHCA.

Since the passage of GLB, the Association for Financial Professionals (AFP) has conducted several surveys exploring credit access. The first survey, conducted in December 2002, looked at the impact that the recent consolidation in the financial industry had on credit access. That survey found that commercial banks required or strongly encouraged companies to grant other financial business to gain short-term credit and, as a result, many companies expected adverse consequences from not awarding other business to short-term credit providers. AFP’s follow-up survey in January 2003 showed increasing pressure to award other banking services in exchange for credit. The 2003 survey also showed that large companies—those with annual revenues greater than \$1 billion—were more likely to have credit access linked to the purchase of other financial services.

The survey results have generated interest from policy makers. In July 2002, Representative Dingell asked the Federal Reserve Board and the Office of the Comptroller of the Currency (OCC) whether commercial banking organizations “tie the availability or price of credit to the purchase of investment banking services.” The agencies previously stated that they had not identified any prohibited tying activity by commercial banks but were undertaking further review.

On August 25, 2003, the Board of Governors of the Federal Reserve System issued a “proposed interpretation and supervisory guidance with request for public comment” on the anti-tying restrictions of the BHCA. The proposal was an attempt to clarify what constitutes permissible tying and what is prohibited. Following the release of the proposal, the Fed announced that they had fined and issued a cease and desist order to WestLB AG, of Germany, for violations of section 106 of the BHCA. In September

2003, the OCC stated in a white paper that there was no empirical evidence indicating that national banks tie lending to underwriting activities.

In October 2003, the General Accounting Office (GAO) reported that it did not find widespread evidence of illegal tying. However, the GAO noted that, due to the nature of negotiations, it is exceedingly difficult to find “documentary evidence” of tying. Further, the GAO noted that the Federal Reserve and the OCC did not review transactions nor talk to customers about possible tying activity. As a result, the GAO recommended that the regulators take additional steps to ensure effective enforcement of existing anti-tying restrictions. GAO recommended that the regulators improve their communication with bank customers and provide a mechanism by which corporate finance professionals could make inquires or file complaints.

After the Federal Reserve, OCC and GAO each released reports that found no evidence of tying activity, AFP once again surveyed senior-level financial professionals. The 13-question survey, conducted in February 2004, measures the prevalence and impact of commercial banks linking credit to the purchase of other financial services and the resultant actions taken by companies in this environment. This survey also includes specific examples of activity that the Federal Reserve has indicated would be prohibited. The responses from 370 financial executives are the basis of this report. At a 95 percent confidence level, the 370 completed surveys produce a confidence interval of ± 5.0 percentage points.

The membership of AFP includes approximately 14,000 financial executives employed by over 5,000 corporations and other organizations. AFP’s members represent a broad spectrum of financial disciplines; their organizations are drawn generally from the Fortune 1000 and middle-market companies in a wide variety of industries, including manufacturing, retail, energy, financial services and technology.

Survey Findings

Financial professionals continue to report that commercial banks frequently make access to credit contingent upon the purchase of other financial services, despite assertions by regulatory bodies to the contrary. Large companies—those with annual revenues greater than \$1 billion—are more likely to be subject to banks’ attempts to link credit access to other financial services. Large companies are more likely to be subject to linking activity, in part because their size and complex credit needs limit the number of commercial banks that are able and willing to serve them. Many respondents indicate that the pressure to award other business continues to increase because there are fewer alternate banks that are able and willing to meet their credit needs as a result of commercial bank consolidation.

Credit as a Stand-Alone Product

Many financial professionals indicate that commercial banks do not always offer (and, therefore, do not price) credit as a stand-alone product. Rather, most survey respondents report that their company must purchase other products to secure credit. Consequently, the “true” cost of credit may be unclear to financial professionals because it is commonly bundled with other products.

Just 44 percent of survey respondents—including 42 percent of those from large companies—report that commercial banks “always” or “usually” offer the option of purchasing credit as a stand-alone offering. **Further, 29 percent of respondents—including 33 percent of those from large companies—indicate that banks “rarely” or “never” offer the option of purchasing credit as a stand-alone offering.**

Companies Offered the Option of Purchasing Credit as a Stand-Alone Offering

(Percentage Distribution)

	Always	Usually	Sometimes	Rarely	Never
All companies	17%	27%	27%	13%	16%
Companies w/ annual revenues greater than \$1 billion	19	23	26	14	19

Denied Credit/Changed Terms

Unable to purchase credit as a stand-alone offering, many financial professionals further indicate that their company’s access to credit has been adversely affected after not purchasing other financial services from a credit bank. **Nearly two-thirds of companies with annual revenues greater than \$1 billion (63 percent) indicate that, over the past five years, a commercial bank has denied them credit or changed credit terms because the company did not award other business to the bank.** Half of respondents from companies of all sizes believe they have been subjected to similar practices.

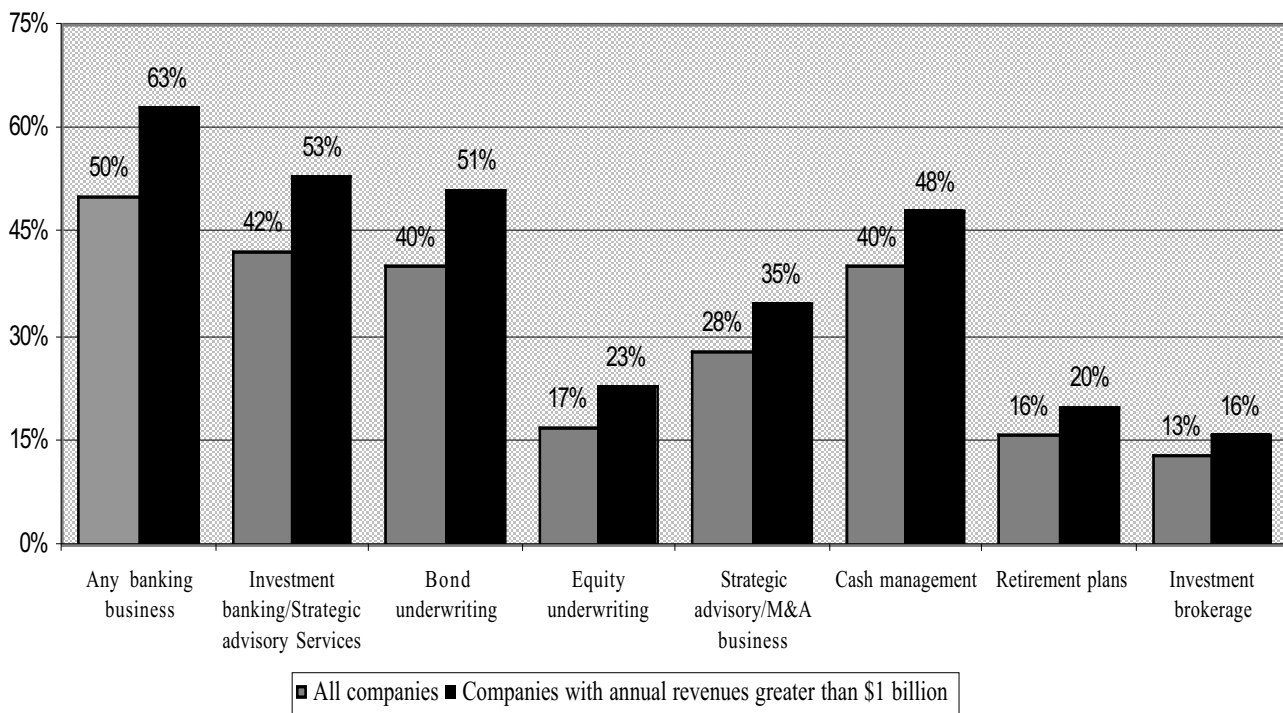
Over half (53 percent) of companies were denied credit or had credit terms changed in the past five years after they did not award investment banking business to a commercial bank. Among users of specific investment banking services:

- Fifty-one percent of large companies had credit denied or terms changed after they did not award bond underwriting business.
- Twenty-three percent of large companies had credit denied or terms changed after they did not award equity underwriting business.
- Thirty-five percent of large companies had credit denied or terms changed after they did not award strategic advisory or merger and acquisition business.

In addition to the services listed above, commercial banks have linked credit to other services. For example, nearly half of respondents from large companies indicate that they have been denied credit or had credit terms changed after not awarding a commercial bank cash management business. Twenty percent and 16 percent of large companies indicate they have been subject to similar practices after not awarding retirement plan and investment brokerage business, respectively.

Companies that Have Been Denied Credit or Had Credit Terms Changed Because They Did Not Award a Commercial Bank Other Business

(Percent of Companies that Purchase Specific Services—Past Five Years)



Explicit Consequences of Not Awarding Other Business

Many financial professionals indicate that a bank was unambiguous for the reason why it decided to deny credit or change credit terms to their company. **A third**

of large companies indicate that a commercial bank has explicitly told them that they were denied credit or had credit terms changed because they did not award the bank other business. Twenty-nine percent of companies, regardless of size, indicate that they were denied credit or had credit terms changed by a commercial bank and were explicitly told by the bank that it took this action because the company did not award it other business.

A quarter of large companies that are users of investment banking services indicate that a commercial bank told them that it withdrew credit or changed credit terms because the companies did not award investment banking business to the bank. The percentages of large companies that are users of the following investment banking services and were explicitly denied credit or had terms changed are:

- Twenty-two percent that use bond underwriting services
- Twelve percent that use equity underwriting services
- Eighteen percent that use strategic advisory services.

Nearly a quarter (23 percent) of large companies lost credit or had terms changed after not awarding cash management. Seven and five percent of large companies, respectively, had a similar outcome after not awarding either retirement plan or investment brokerage business.

Companies that Have Been Denied Credit or Had Credit Terms Changed Explicitly Because They Did Not Award a Commercial Bank Other Business

(Percent of Companies that Purchase Specific Services—Past Five Years)

	All Companies	Companies with annual revenues greater than \$1 billion
Any banking business	29%	33%
Investment banking/Strategic advisory services	22	25
Bond underwriting	20	22
Equity underwriting	11	12
Strategic underwriting/M&A business	15	18
Cash management	22	23
Retirement plans	6	7
Investment brokerage	6	5

Implicit Consequences of Not Awarding Other Business

In other cases, companies indicate that a commercial bank was not as overt as to why they were denied credit or had credit terms changed. **Fifty-nine percent of respondents from large companies report that a commercial bank implied that they were denied credit or had credit terms changed because the company did not award the bank other business.** Forty-four percent of companies of all sizes report that a commercial bank engaged in similar activity.

Nearly half (49 percent) of large companies indicate that they were denied credit or had credit terms changed by a commercial bank that implied the reason was the failure of the company to award investment banking business. The percentages of large companies to which a commercial bank implied that it denied credit or changed credit terms because it was not awarded investment banking business are:

- Forty-eight percent that use bond underwriting services
- Twenty-one percent that use equity underwriting services
- Thirty-three percent that use strategic advisory services.

Among other non-investment banking services, the percentages of large companies to which a commercial bank implied that it denied credit or changed credit terms because it was not awarded other business are:

- Forty-four percent that use cash management services
- Nineteen percent that use retirement plan services
- Sixteen percent that use investment brokerage services.

Companies that Have Been Denied Credit or Had Credit Terms Changed Implicitly Because They Did Not Award a Commercial Bank Other Business

(Percent of Companies that Purchase Specific Services—Past Five Years)

	All Companies	Companies with annual revenues greater than \$1 billion
Any banking business	44%	59%
Investment banking/Strategic advisory services	37	49
Bond underwriting	36	48
Equity underwriting	14	21
Strategic underwriting/M&A business	25	33
Cash management	35	44
Retirement plans	15	19
Investment brokerage	13	16

2003 Federal Reserve Interpretation

In August 2003, the Federal Reserve Board proposed an interpretation of the anti-tying restrictions of Section 106 of the Bank Holding Company Act Amendments of 1970 and related supervisory guidance. The draft interpretation included specific actions and scenarios that the Federal Reserve would consider to be a “prohibited tying” arrangement.

In its interpretation, the Federal Reserve states that “a bank would violate section 106 if the bank informs a customer seeking only a loan from the bank that the bank will make the loan only if the customer commits to hire the bank’s securities affiliate to underwrite an upcoming bond offering for the customer.” **One out of seven large companies**

(15 percent) report that in the past five years they have been explicitly required by a commercial bank to obtain corporate debt and/or equity underwriting services from an affiliate of the bank in order to obtain a loan from the bank. Fourteen percent of companies of all sizes indicate that they were subject to similar requirements. While a bank’s requirement may have been explicit, it typically was not put in writing. Three-quarters of the survey respondents indicate that the requirement was expressed only verbally.

Companies that Have Been Explicitly Required by a Bank to Obtain Corporate Debt and/or Equity Underwriting Services from an Affiliate of the Bank in Order to Obtain a Loan

(Percent of Companies that Use Underwriting Services—Past Five Years)

All companies	Companies with annual revenues greater than \$1 billion
14%	15%

Many banks impose minimum fee requirements on their customers seeking credit. **A third of large companies have been told by a commercial bank that they would have to provide a specific amount of fee income in order to be granted credit.** A quarter of all responding companies indicate that they have been subject to revenue targets.

Companies that Have Been Told by their Bank to Provide a Specific Amount of Fee Income to Be Granted Credit

(Percent of Companies—Past Five Years)

All companies	Companies with annual revenues greater than \$1 billion
25%	34%

The Federal Reserve interpretation does not prohibit giving companies a specific target for banking fee income to secure credit so long as the company has a “meaningful option” to satisfy the bank’s condition solely through the purchase of “traditional bank products.” **However, more than half of large companies indicate that they cannot meet revenue targets imposed by a credit bank without awarding bond or equity underwriting and/or strategic advisory services.**

Companies that Must Award Underwriting or Strategic Advisory Services To Meet Requested Fee Income Target

(Percentage Distribution of Companies That Must Meet a Revenue Target)

	All companies	Companies with annual revenues greater than \$1 billion
Company must award underwriting or strategic advisory services to meet all or some of the requested fee income	49%	52%
Company could meet revenue target without awarding underwriting or strategic advisory services	51	48

The Federal Reserve’s interpretation notes that Section 106 prohibits a bank from setting up an “exclusive dealing” arrangement in which it bars a customer from obtaining another product from a competing bank. It states “this restriction, for example, prohibits a bank that has a securities affiliate engaged in bond underwriting activities from threatening a corporate customer that the bank will terminate the bank’s credit relationships with the customer if the customer uses the bond underwriting services of a competitor of the bank’s securities affiliate.” **More than a quarter of respondents from large companies indicate that they have been subject to exclusive dealing requirements from a commercial bank.**

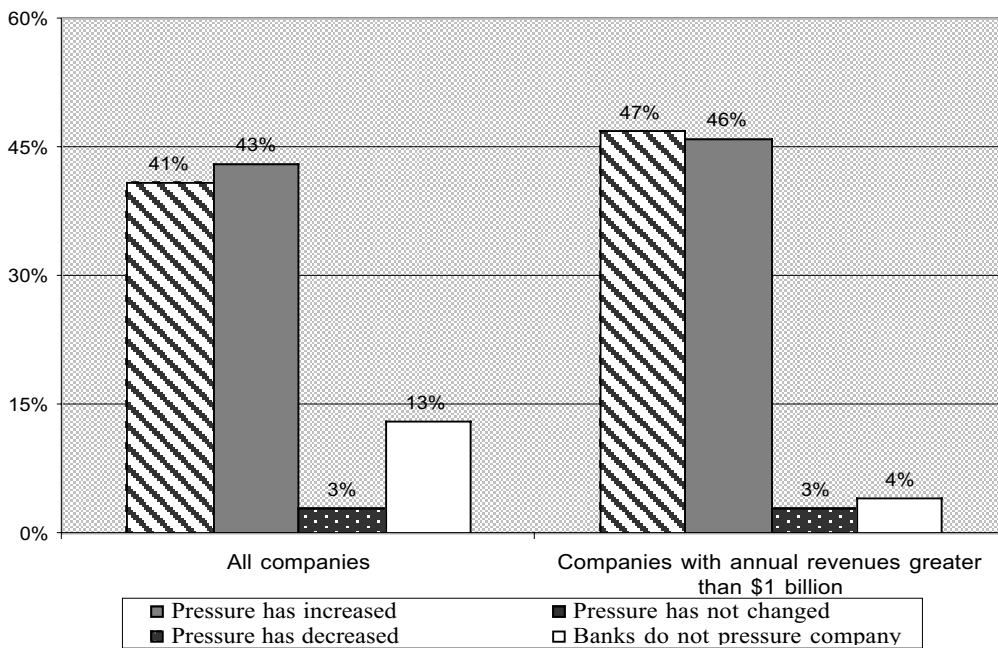
Companies Threatened by a Bank with Termination of Their Credit Relationships If They Were to Use a Competitor’s Underwriting Services
(Percent of Companies that Use Underwriting Services)

All companies	Companies with annual revenues greater than \$1 billion
21%	28%

Increasing Pressure to Award Other Business

Ninety-six percent of respondents from large companies report that their company is subject to pressure from their credit providers to award other business. **Forty-seven percent of large companies have been subject to increasing pressure to award additional business over the last year.** Two out of five companies of all sizes indicate that this pressure has increased over the past year.

Change in Pressure on Companies to Award Other Business in the Past Year
(Percentage Distribution)



Anticipated Consequences of Not Awarding Other Business

Many financial professionals believe that their company would not be able to secure credit, or would have to pay more for it, should it decide to not award other business to a credit provider. These include financial professionals who did not indicate that their company had lost credit or had credit terms changed after not awarding other business.

Ninety percent of respondents from large companies expect to be denied credit, or pay more for credit, should they not award other business to a commercial bank.

According to respondents from large companies, the anticipated consequences of not awarding other business to a commercial bank are:

- The bank(s) would not provide credit in the future (46%)
- The bank(s) would reduce the amount of credit provided (64%)
- The bank(s) would continue to provide credit, but at a higher rate (29%)

Anticipated Consequences of Not Awarding Business to a Commercial Bank

(Percent of Respondents)

	All companies	Companies with annual revenues greater than \$1 billion
The bank would not provide credit in the future	34%	46%
The bank would reduce the amount of credit already provided	42	64
The bank would continue to provide credit, but would charge a higher rate	36	29
Other impact	2	2
No impact on company's relationship with the bank	22	10

Commercial Bank Consolidation

The pressure to award additional business has increased at the same time the number of commercial banks from which a company can purchase credit has decreased. Financial professionals report that their company has fewer options for commercial credit, due to commercial bank consolidation. Because of their size and the complexity of their credit needs, large companies are more likely to indicate that they have fewer choices for credit banks. **Nearly three out of five respondents from large companies (57 percent) report that the number of banks that are willing and able to meet their company's credit needs has decreased over the past five years.** Only twenty-seven percent of respondents from large companies indicate that there are more banks that are willing and able to meet their company's credit needs. Forty-three percent of respondents from companies of any size also report a decrease in the number of willing and able banks.

Change in the Number of Banks Willing and Able to Meet Companies' Credit Needs Over the Past Five Years

(Percentage Distribution)

	All companies	Companies with annual revenues greater than \$1 billion
Significant decrease	11%	15%
Some decrease	32	42
No change	23	17
Some increase	27	21
Significant increase	7	6

Financial professionals are concerned about the impact of bank mergers and industry consolidation. Eighty-five percent expect banks to gain greater negotiating power as a result of consolidation. More than three-fourths of large company respondents believe the availability of credit will decrease while the price of the remaining credit will increase. Sixty-three percent of financial professionals from large companies expect to pay higher prices for cash management services as a result of mergers.

Still, financial professionals do envision some benefits from banking industry consolidation. For example, 40 percent of large company respondents expect to benefit from the convenience that will arise from the expanded footprint of national banks. Also, a third of large company respondents believe larger banks will have a greater incentive to innovate in their treasury and cash management services offerings.

Financial Professionals' Perceived Impact of Increasing Banking Consolidation on Commercial Banking Services

(Percentage of Respondents)

	All companies	Companies with annual revenues greater than \$1 billion
Greater negotiating power held by commercial banks	76%	85%
Higher priced bank credit	73	76
Higher prices for cash management services	69	63
Decreased credit availability	58	77
Greater innovation in treasury/cash management services	39	33
Greater convenience from extended branch networks	38	40
Less innovation in treasury/cash management services	25	31
No significant impact expected	14	15
Increased credit availability	8	4
Lower prices for cash management services	8	10
Lower priced bank credit	3	2
Less negotiating power held by commercial banks	3	2

Conclusions

Financial professionals report that their companies have been denied credit or had credit terms changed by a commercial bank because the company did not award other financial business, despite assertions by regulators to the contrary. Large companies, which tend to have fewer options for commercial bank credit because of their size and complex credit needs, are more likely to be subject to such activity. Among the services that commercial banks link to credit access are investment banking services, including bond and equity underwriting and strategic advisory services. A significant percentage of survey respondents note that their company has been subject to activities that the Federal Reserve indicates would violate Section 106 of the Bank Holding Company Act. Further, many companies continue to report that the pressure to award business has increased over the past year. Financial professionals also express concern that, as a result of consolidation among large commercial banks, their companies have fewer banks that are willing and able to meeting their company's credit needs.

About the Association for Financial Professionals

The Association for Financial Professionals (AFP) headquartered in Bethesda, Maryland, supports more than 14,000 individual members from a wide range of industries throughout all stages of their careers in various aspects of treasury and financial management. AFP is the preferred resource for financial professionals for continuing education, financial tools and publications, career development, certifications, research, representation to legislators and regulators, and the development of industry standards.

General Inquiries: AFP@AFPonline.org

Web Site: www.AFPonline.org

Phone: 301.907.2862