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CONDITIONS TO ORDERS

225.200 Conditions to Board's section 20 orders.

APPENDIX A TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: RISK-BASED MEASURE

APPENDIX B TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES AND STATE MEMBER BANKS: LEVERAGE MEASURE

APPENDIX C TO PART 225—SMALL BANK HOLDING COMPANY POLICY STATEMENT

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APPENDIX F TO PART 225—INTERAGENCY GUIDELINES ESTABLISHING INFORMATION SECURITY STANDARDS

APPENDIX G TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: INTERNAL-RATINGS-BASED AND ADVANCED MEASUREMENT APPROACHES

AUTHORITY: 12 U.S.C. 1817(j)(13), 1818, 1828(o), 1831i, 1831p–1, 1843(c)(8), 1844(b), 1972(1), 3106, 3108, 3310, 3331–3351, 3906, 3907, and 3909; 15 U.S.C. 1681s, 1681w, 6801 and 6805.

SOURCE: Reg. Y, 49 FR 818, Jan. 5, 1984, unless otherwise noted.

EDITORIAL NOTE: Nomenclature changes for part 225 appear at 69 FR 77618, Dec. 28, 2004.

REGULATIONS

Subpart A—General Provisions

SOURCE: Reg. Y, 62 FR 9319, Feb. 28, 1997, unless otherwise noted.

§ 225.1 Authority, purpose, and scope.

(a) *Authority.* This part[1] (Regulation Y) is issued by the Board of Governors of the Federal Reserve System (*Board*) under section 5(b) of the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1844(b)) (*BHC Act*); sections 8 and 13(a) of the International Banking Act of 1978 (12 U.S.C. 3106 and 3108); section 7(j)(13) of the Federal Deposit Insurance Act, as amended by the Change in Bank Control Act of 1978 (12 U.S.C. 1817(j)(13)) (*Bank Control Act*); section 8(b) of the Federal Deposit Insurance Act (12 U.S.C. 1818(b)); section 914 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (12 U.S.C. 1831i); section 106 of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. 1972); and the International Lending Supervision Act of 1983 (Pub. L. 98–181, title IX). The BHC Act is codified at 12 U.S.C. 1841, *et seq.*

(b) *Purpose.* The principal purposes of this part are to:

(1) Regulate the acquisition of control of banks by companies and individuals;

(2) Define and regulate the nonbanking activities in which bank holding companies and foreign banking organizations with United States operations may engage; and

(3) Set forth the procedures for securing approval for these transactions and activities.

(c) *Scope*—(1) *Subpart A* contains general provisions and definitions of terms used in this regulation.

(2) *Subpart B* governs acquisitions of bank or bank holding company securities and assets by bank holding companies or by any company that will become a bank holding company as a result of the acquisition.

(3) *Subpart C* defines and regulates the nonbanking activities in which bank holding companies and foreign banking organizations may engage directly or through a subsidiary. The Board's Regulation K governs certain nonbanking activities conducted by foreign banking organizations and certain foreign activities conducted by bank holding companies (12 CFR part 211, International Banking Operations).

(4) *Subpart D* specifies situations in which a company is presumed to control voting securities or to have the power to exercise a controlling influence over the management or policies of a bank or other company; sets forth the procedures for making a control determination; and provides rules governing the effectiveness of divestitures by bank holding companies.

(5) *Subpart E* governs changes in bank control resulting from the acquisition by individuals or companies (other than bank holding companies) of voting securities of a bank holding company or state member bank of the Federal Reserve System.

(6) *Subpart F* specifies the limitations that govern companies that control so-

[1] Code of Federal Regulations, title 12, chapter II, part 225.

called nonbank banks and the activities of nonbank banks.

(7) *Subpart G* prescribes minimum standards that apply to the performance of real estate appraisals and identifies transactions that require state certified appraisers.

(8) *Subpart H* identifies the circumstances when written notice must be provided to the Board prior to the appointment of a director or senior officer of a bank holding company and establishes procedures for obtaining the required Board approval.

(9) Subpart I establishes the procedure by which a bank holding company may elect to become a financial holding company, enumerates the consequences if a financial holding company ceases to meet a requirement applicable to a financial holding company, lists the activities in which a financial holding company may engage, establishes the procedure by which a person may request the Board to authorize additional activities as financial in nature or incidental thereto, and establishes the procedure by which a financial holding company may seek approval to engage in an activity that is complementary to a financial activity.

(10) *Subpart J* governs the conduct of merchant banking investment activities by financial holding companies as permitted under section 4(k)(4)(H) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(H)).

(11) *Appendix A* to the regulation contains the Board's Risk-Based Capital Adequacy Guidelines for bank holding companies.

(12) *Appendix B* contains the Board's Capital Adequacy Guidelines for measuring leverage for bank holding companies and state member banks.

(13) *Appendix C* contains the Board's policy statement governing small bank holding companies.

(14) *Appendix D* contains the Board's Capital Adequacy Guidelines for measuring tier 1 leverage for bank holding companies.

(15) *Appendix E* contains the Board's Capital Adequacy Guidelines for measuring market risk of bank holding companies.

(16) *Appendix F* contains the Interagency Guidelines Establishing Information Security Standards.

[Reg. Y, 62 FR 9319, Feb. 28, 1997, as amended at 65 FR 16472, Mar. 28, 2000; 66 FR 414, Jan. 3, 2001; 66 FR 8484, Jan. 31, 2001; 66 FR 8636, Feb. 1, 2001]

§ 225.2 Definitions.

Except as modified in this regulation or unless the context otherwise requires, the terms used in this regulation have the same meaning as set forth in the relevant statutes.

(a) *Affiliate* means any company that controls, is controlled by, or is under common control with, another company.

(b)(1) *Bank* means:

(i) An insured bank as defined in section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)); or

(ii) An institution organized under the laws of the United States which both:

(A) Accepts demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others; and

(B) Is engaged in the business of making commercial loans.

(2) *Bank* does not include those institutions qualifying under the exceptions listed in section 2(c)(2) of the BHC Act (12 U.S.C. 1841(c)(2)).

(c)(1) *Bank holding company* means any company (including a bank) that has direct or indirect control of a bank, other than control that results from the ownership or control of:

(i) Voting securities held in good faith in a fiduciary capacity (other than as provided in paragraphs (e)(2)(ii) and (iii) of this section) without sole discretionary voting authority, or as otherwise exempted under section 2(a)(5)(A) of the BHC Act;

(ii) Voting securities acquired and held only for a reasonable period of time in connection with the underwriting of securities, as provided in section 2(a)(5)(B) of the BHC Act;

(iii) Voting rights to voting securities acquired for the sole purpose and in the course of participating in a proxy solicitation, as provided in section 2(a)(5)(C) of the BHC Act;

(iv) Voting securities acquired in satisfaction of debts previously contracted in good faith, as provided in section 2(a)(5)(D) of the BHC Act, if the securities are divested within two years of acquisition (or such later period as the Board may permit by order); or

(v) Voting securities of certain institutions owned by a thrift institution or a trust company, as provided in sections 2(a)(5)(E) and (F) of the BHC Act.

(2) Except for the purposes of § 225.4(b) of this subpart and subpart E of this part, or as otherwise provided in this regulation, *bank holding company* includes a foreign banking organization. For the purposes of subpart B of this part, *bank holding company* includes a foreign banking organization only if it owns or controls a bank in the United States.

(d)(1) *Company* includes any bank, corporation, general or limited partnership, association or similar organization, business trust, or any other trust unless by its terms it must terminate either within 25 years, or within 21 years and 10 months after the death of individuals living on the effective date of the trust.

(2) *Company* does not include any organization, the majority of the voting securities of which are owned by the United States or any state.

(3) *Testamentary trusts exempt.* Unless the Board finds that the trust is being operated as a business trust or company, a trust is presumed not to be a company if the trust:

(i) Terminates within 21 years and 10 months after the death of grantors or beneficiaries of the trust living on the effective date of the trust or within 25 years;

(ii) Is a testamentary or *inter vivos* trust established by an individual or individuals for the benefit of natural persons (or trusts for the benefit of natural persons) who are related by blood, marriage or adoption;

(iii) Contains only assets previously owned by the individual or individuals who established the trust;

(iv) Is not a Massachusetts business trust; and

(v) Does not issue shares, certificates, or any other evidence of ownership.

(4) *Qualified limited partnerships exempt.* Company does not include a qualified limited partnership, as defined in section 2(o)(10) of the BHC Act.

(e)(1) *Control* of a bank or other company means (except for the purposes of subpart E of this part):

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting securities of the bank or other company, directly or indirectly or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of the bank or other company;

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of the bank or other company, as determined by the Board after notice and opportunity for hearing in accordance with § 225.31 of subpart D of this part; or

(iv) Conditioning in any manner the transfer of 25 percent or more of the outstanding shares of any class of voting securities of a bank or other company upon the transfer of 25 percent or more of the outstanding shares of any class of voting securities of another bank or other company.

(2) A bank or other company is deemed to control voting securities or assets owned, controlled, or held, directly or indirectly:

(i) By any subsidiary of the bank or other company;

(ii) In a fiduciary capacity (including by pension and profit-sharing trusts) for the benefit of the shareholders, members, or employees (or individuals serving in similar capacities) of the bank or other company or any of its subsidiaries; or

(iii) In a fiduciary capacity for the benefit of the bank or other company or any of its subsidiaries.

(f) *Foreign banking organization* and *qualifying foreign banking organization* have the same meanings as provided in § 211.21(n) and § 211.23 of the Board's Regulation K (12 CFR 211.21(n) and 211.23).

(g) *Insured depository institution* includes an insured bank as defined in

section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)) and a savings association.

(h) *Lead insured depository institution* means the largest insured depository institution controlled by the bank holding company as of the quarter ending immediately prior to the proposed filing, based on a comparison of the average total risk-weighted assets controlled during the previous 12-month period by each insured depository institution subsidiary of the holding company.

(i) *Management official* means any officer, director (including honorary or advisory directors), partner, or trustee of a bank or other company, or any employee of the bank or other company with policy-making functions.

(j) *Nonbank bank* means any institution that:

(1) Became a bank as a result of enactment of the Competitive Equality Amendments of 1987 (Pub. L. 100–86), on the date of enactment (August 10, 1987); and

(2) Was not controlled by a bank holding company on the day before the enactment of the Competitive Equality Amendments of 1987 (August 9, 1987).

(k) *Outstanding shares* means any voting securities, but does not include securities owned by the United States or by a company wholly owned by the United States.

(l) Person includes an individual, bank, corporation, partnership, trust, association, joint venture, pool, syndicate, sole proprietorship, unincorporated organization, or any other form of entity.

(m) *Savings association* means:

(1) Any federal savings association or federal savings bank;

(2) Any building and loan association, savings and loan association, homestead association, or cooperative bank if such association or cooperative bank is a member of the Savings Association Insurance Fund; and

(3) Any savings bank or cooperative that is deemed by the director of the Office of Thrift Supervision to be a savings association under section 10(l) of the Home Owners Loan Act.

(n) *Shareholder*—(1) *Controlling shareholder* means a person that owns or controls, directly or indirectly, 25 percent or more of any class of voting securities of a bank or other company.

(2) *Principal shareholder* means a person that owns or controls, directly or indirectly, 10 percent or more of any class of voting securities of a bank or other company, or any person that the Board determines has the power, directly or indirectly, to exercise a controlling influence over the management or policies of a bank or other company.

(o) *Subsidiary* means a bank or other company that is controlled by another company, and refers to a direct or indirect subsidiary of a bank holding company. An indirect subsidiary is a bank or other company that is controlled by a subsidiary of the bank holding company.

(p) *United States* means the United States and includes any state of the United States, the District of Columbia, any territory of the United States, Puerto Rico, Guam, American Samoa, and the Virgin Islands.

(q)(1) *Voting securities* means shares of common or preferred stock, general or limited partnership shares or interests, or similar interests if the shares or interest, by statute, charter, or in any manner, entitle the holder:

(i) To vote for or to select directors, trustees, or partners (or persons exercising similar functions of the issuing company); or

(ii) To vote on or to direct the conduct of the operations or other significant policies of the issuing company.

(2) *Nonvoting shares.* Preferred shares, limited partnership shares or interests, or similar interests are not *voting securities* if:

(i) Any voting rights associated with the shares or interest are limited solely to the type customarily provided by statute with regard to matters that would significantly and adversely affect the rights or preference of the security or other interest, such as the issuance of additional amounts or classes of senior securities, the modification of the terms of the security or interest, the dissolution of the issuing company, or the payment of dividends by the issuing company when preferred dividends are in arrears;

(ii) The shares or interest represent an essentially passive investment or financing device and do not otherwise provide the holder with control over the issuing company; and

(iii) The shares or interest do not entitle the holder, by statute, charter, or in any manner, to select or to vote for the selection of directors, trustees, or partners (or persons exercising similar functions) of the issuing company.

(3) *Class of voting shares.* Shares of stock issued by a single issuer are deemed to be the same class of voting shares, regardless of differences in dividend rights or liquidation preference, if the shares are voted together as a single class on all matters for which the shares have voting rights other than matters described in paragraph (o)(2)(i) of this section that affect solely the rights or preferences of the shares.

(r) *Well-capitalized*—(1) *Bank holding company.* In the case of a bank holding company,[2] *well-capitalized* means that:

(i) On a consolidated basis, the bank holding company maintains a total risk-based capital ratio of 10.0 percent or greater, as defined in appendix A of this part;

(ii) On a consolidated basis, the bank holding company maintains a Tier 1 risk-based capital ratio of 6.0 percent or greater, as defined in appendix A of this part; and

(iii) The bank holding company is not subject to any written agreement, order, capital directive, or prompt corrective action directive issued by the Board to meet and maintain a specific capital level for any capital measure.

(2) *Insured and uninsured depository institution*—(i) *Insured depository institution.* In the case of an insured depository institution, ''well capitalized'' means that the institution has and maintains at least the capital levels required to be well capitalized under the capital adequacy regulations or guidelines applicable to the institution that have been adopted by the appropriate Federal banking agency for the institution under section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o).

(ii) *Uninsured depository institution.* In the case of a depository institution the deposits of which are not insured by the Federal Deposit Insurance Corporation, ''well capitalized'' means that the institution has and maintains at least the capital levels required for an insured depository institution to be well capitalized.

(3) *Foreign banks*—(i) *Standards applied.* For purposes of determining whether a foreign banking organization qualifies under paragraph (r)(1) of this section:

(A) A foreign banking organization whose home country supervisor, as defined in §211.21 of the Board's Regulation K (12 CFR 211.21), has adopted capital standards consistent in all respects with the Capital Accord of the Basle Committee on Banking Supervision (Basle Accord) may calculate its capital ratios under the home country standard; and

(B) A foreign banking organization whose home country supervisor has not adopted capital standards consistent in all respects with the Basle Accord shall obtain a determination from the Board that its capital is equivalent to the capital that would be required of a U.S. banking organization under paragraph (r)(1) of this section.

(ii) *Branches and agencies.* For purposes of determining, under paragraph (r)(1) of this section, whether a branch or agency of a foreign banking organization is well-capitalized, the branch or agency shall be deemed to have the same capital ratios as the foreign banking organization.

(s) *Well managed*—(1) *In general.* Except as otherwise provided in this part, a company or depository institution is well managed if:

(i) At its most recent inspection or examination or subsequent review by the appropriate Federal banking agency for the company or institution (or the appropriate state banking agency in an examination described in section 10(d) of the Federal Deposit Insurance Act (12 U.S.C. 1820(d)), the company or institution received:

[2] For purposes of this subpart and subparts B and C of this part, a bank holding company with consolidated assets of less than $500 million that is subject to the Small Bank Holding Company Policy Statement in Appendix C of this part will be deemed to be ''well-capitalized'' if the bank holding company meets the requirements for expedited/waived processing in Appendix C.

(A) At least a satisfactory composite rating; and

(B) At least a satisfactory rating for management, if such rating is given.

(ii) In the case of a company or depository institution that has not received an inspection or examination rating, the Board has determined, after a review of the managerial and other resources of the company or depository institution and after consulting with the appropriate Federal and state banking agencies, as applicable, for the company or institution, that the company or institution is well managed.

(2) *Merged depository institutions*—(i) *Merger involving well managed institutions.* A depository institution that results from the merger of two or more depository institutions that are well managed shall be considered to be well managed unless the Board determines otherwise after consulting with the appropriate Federal and state banking agencies, as applicable, for each depository institution involved in the merger.

(ii) *Merger involving a poorly rated institution.* A depository institution that results from the merger of a depository institution that is well managed with one or more depository institutions that are not well managed or have not been examined shall be considered to be well managed if the Board determines, after a review of the managerial and other resources of the resulting depository institution and after consulting with the appropriate Federal and state banking agencies for the institutions involved in the merger, as applicable, that the resulting institution is well managed.

(3) *Foreign banking organizations.* Except as otherwise provided in this part, a foreign banking organization is considered well managed if the combined operations of the foreign banking organization in the United States have received at least a satisfactory composite rating at the most recent annual assessment.

(t) *Depository institution.* For purposes of this part, the term ''depository institution'' has the same meaning as in section 3(c) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)).

[Reg. Y, 62 FR 9319, Feb. 28, 1997, as amended at 65 FR 3791, Jan. 25, 2000; 65 FR 15055, Mar. 21, 2000; 66 FR 414, Jan. 3, 2001; 71 FR 9901, Feb. 28, 2006]

§ 225.3 Administration.

(a) *Delegation of authority.* Designated Board members and officers and the Federal Reserve Banks are authorized by the Board to exercise various functions prescribed in this regulation and in the Board's Rules Regarding Delegation of Authority (12 CFR part 265) and the Board's Rules of Procedure (12 CFR part 262).

(b) *Appropriate Federal Reserve Bank.* In administering this regulation, unless a different Federal Reserve Bank is designated by the Board, the appropriate Federal Reserve Bank is as follows:

(1) For a bank holding company (or a company applying to become a bank holding company): the Reserve Bank of the Federal Reserve district in which the company's banking operations are principally conducted, as measured by total domestic deposits in its subsidiary banks on the date it became (or will become) a bank holding company;

(2) For a foreign banking organization that has no subsidiary bank and is not subject to paragraph (b)(1) of this section: the Reserve Bank of the Federal Reserve district in which the total assets of the organization's United States branches, agencies, and commercial lending companies are the largest as of the later of January 1, 1980, or the date it becomes a foreign banking organization;

(3) For an individual or company submitting a notice under subpart E of this part: The Reserve Bank of the Federal Reserve district in which the banking operations of the bank holding company or state member bank to be acquired are principally conducted, as measured by total domestic deposits on the date the notice is filed.

§ 225.4 Corporate practices.

(a) *Bank holding company policy and operations.* (1) A bank holding company shall serve as a source of financial and managerial strength to its subsidiary

banks and shall not conduct its operations in an unsafe or unsound manner.

(2) Whenever the Board believes an activity of a bank holding company or control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) constitutes a serious risk to the financial safety, soundness, or stability of a subsidiary bank of the bank holding company and is inconsistent with sound banking principles or the purposes of the BHC Act or the Financial Institutions Supervisory Act of 1966, as amended (12 U.S.C. 1818(b) *et seq.*), the Board may require the bank holding company to terminate the activity or to terminate control of the subsidiary, as provided in section 5(e) of the BHC Act.

(b) *Purchase or redemption by bank holding company of its own securities*—(1) *Filing notice.* Except as provided in paragraph (b)(6) of this section, a bank holding company shall give the Board prior written notice before purchasing or redeeming its equity securities if the gross consideration for the purchase or redemption, when aggregated with the net consideration paid by the company for all such purchases or redemptions during the preceding 12 months, is equal to 10 percent or more of the company's consolidated net worth. For the purposes of this section, ''net consideration'' is the gross consideration paid by the company for all of its equity securities purchased or redeemed during the period minus the gross consideration received for all of its equity securities sold during the period.

(2) *Contents of notice.* Any notice under this section shall be filed with the appropriate Reserve Bank and shall contain the following information:

(i) The purpose of the transaction, a description of the securities to be purchased or redeemed, the total number of each class outstanding, the gross consideration to be paid, and the terms and sources of funding for the transaction;

(ii) A description of all equity securities redeemed within the preceding 12 months, the net consideration paid, and the terms of any debt incurred in connection with those transactions; and

(iii) (A) If the bank holding company has consolidated assets of $500 million or more, consolidated *pro forma* risk-based capital and leverage ratio calculations for the bank holding company as of the most recent quarter, and, if the redemption is to be debt funded, a parent-only *pro forma* balance sheet as of the most recent quarter; or

(B) If the bank holding company has consolidated assets of less than $500 million, a *pro forma* parent-only balance sheet as of the most recent quarter, and, if the redemption is to be debt funded, one-year income statement and cash flow projections.

(3) *Acting on notice.* Within 15 calendar days of receipt of a notice under this section, the appropriate Reserve Bank shall either approve the transaction proposed in the notice or refer the notice to the Board for decision. If the notice is referred to the Board for decision, the Board shall act on the notice within 30 calendar days after the Reserve Bank receives the notice.

(4) *Factors considered in acting on notice.* (i) The Board may disapprove a proposed purchase or redemption if it finds that the proposal would constitute an unsafe or unsound practice, or would violate any law, regulation, Board order, directive, or any condition imposed by, or written agreement with, the Board.

(ii) In determining whether a proposal constitutes an unsafe or unsound practice, the Board shall consider whether the bank holding company's financial condition, after giving effect to the proposed purchase or redemption, meets the financial standards applied by the Board under section 3 of the BHC Act, including the Board's Capital Adequacy Guidelines (Appendix A of this part) and the Board's Policy Statement for Small Bank Holding Companies (Appendix C of this part).

(5) *Disapproval and hearing.* (i) The Board shall notify the bank holding company in writing of the reasons for a decision to disapprove any proposed purchase or redemption. Within 10 calendar days of receipt of a notice of disapproval by the Board, the bank holding company may submit a written request for a hearing.

(ii) The Board shall order a hearing within 10 calendar days of receipt of

the request if it finds that material facts are in dispute, or if it otherwise appears appropriate. Any hearing conducted under this paragraph shall be held in accordance with the Board's Rules of Practice for Formal Hearings (12 CFR part 263).

(iii) At the conclusion of the hearing, the Board shall by order approve or disapprove the proposed purchase or redemption on the basis of the record of the hearing.

(6) *Exception for well-capitalized bank holding companies.* A bank holding company is not required to obtain prior Board approval for the redemption or purchase of its equity securities under this section provided:

(i) Both before and immediately after the redemption, the bank holding company is well-capitalized;

(ii) The bank holding company is well-managed; and

(iii) The bank holding company is not the subject of any unresolved supervisory issues.

(c) *Deposit insurance.* Every bank that is a bank holding company or a subsidiary of a bank holding company shall obtain Federal Deposit Insurance and shall remain an *insured bank* as defined in section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)).

(d) *Acting as transfer agent or clearing agent.* A bank holding company or any nonbanking subsidiary that is a ''bank,'' as defined in section 3(a)(6) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(6)), and that is a transfer agent of securities, a clearing agency, or a participant in a clearing agency (as those terms are defined in section 3(a) of the Securities Exchange Act (15 U.S.C. 78c(a)), shall be subject to §§ 208.31–208.33 of the Board's Regulation H (12 CFR 208.31–208.33) as if it were a state member bank.

(e) *Reporting requirement for credit secured by certain bank holding company stock.* Each executive officer or director of a bank holding company the shares of which are not publicly traded shall report annually to the board of directors of the bank holding company the outstanding amount of any credit that was extended to the executive officer or director and that is secured by shares of the bank holding company. For purposes of this paragraph, the terms ''executive officer'' and ''director'' shall have the meaning given in § 215.2 of Regulation O (12 CFR 215.2).

(f) *Suspicious activity report.* A bank holding company or any nonbank subsidiary thereof, or a foreign bank that is subject to the BHC Act or any nonbank subsidiary of such foreign bank operating in the United States, shall file a suspicious activity report in accordance with the provisions of § 208.62 of the Board's Regulation H (12 CFR 208.62).

(g) *Requirements for financial holding companies engaged in securities underwriting, dealing, or market-making activities.* (1) Any intra-day extension of credit by a bank or thrift, or U.S. branch or agency of a foreign bank to an affiliated company engaged in underwriting, dealing in, or making a market in securities pursuant to section 4(k)(4)(E) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(E)) must be on market terms consistent with section 23B of the Federal Reserve Act. (12 U.S.C. 371c–1).

(2) A foreign bank that is or is treated as a financial holding company under this part shall ensure that:

(i) Any extension of credit by any U.S. branch or agency of such foreign bank to an affiliated company engaged in underwriting, dealing in, or making a market in securities pursuant to section 4(k)(4)(E) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(E)), conforms to sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1) as if the branch or agency were a member bank;

(ii) Any purchase by any U.S. branch or agency of such foreign bank, as principal or fiduciary, of securities for which a securities affiliate described in paragraph (g)(2)(i) of this section is a principal underwriter conforms to sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1) as if the branch or agency were a member bank; and

(iii) Its U.S. branches and agencies not advertise or suggest that they are responsible for the obligations of a securities affiliate described in paragraph (g)(2)(i) of this section, consistent with section 23B(c) of the Federal Reserve Act (12 U.S.C. 371c–1(c)) as

if the branches or agencies were member banks.

(h) *Protection of customer information and consumer information.* A bank holding company shall comply with the Interagency Guidelines Establishing Information Security Standards, as set forth in appendix F of this part, prescribed pursuant to sections 501 and 505 of the Gramm-Leach-Bliley Act (15 U.S.C. 6801 and 6805). A bank holding company shall properly dispose of consumer information in accordance with the rules set forth at 16 CFR part 682.

[Reg. Y, 62 FR 9319, Feb. 28, 1997, as amended at 63 FR 58621, Nov. 2, 1998; 65 FR 14442, Mar. 17, 2000; 66 FR 8636, Feb. 1, 2001; 69 FR 77618, Dec. 28, 2004; 71 FR 9901, Feb. 28, 2006]

§ 225.5 Registration, reports, and inspections.

(a) *Registration of bank holding companies.* Each company shall register within 180 days after becoming a bank holding company by furnishing information in the manner and form prescribed by the Board. A company that receives the Board's prior approval under subpart B of this part to become a bank holding company may complete this registration requirement through submission of its first annual report to the Board as required by paragraph (b) of this section.

(b) *Reports of bank holding companies.* Each bank holding company shall furnish, in the manner and form prescribed by the Board, an annual report of the company's operations for the fiscal year in which it becomes a bank holding company, and for each fiscal year during which it remains a bank holding company. Additional information and reports shall be furnished as the Board may require.

(c) *Examinations and inspections.* The Board may examine or inspect any bank holding company and each of its subsidiaries and prepare a report of their operations and activities. With respect to a foreign banking organization, the Board may also examine any branch or agency of a foreign bank in any state of the United States and may examine or inspect each of the organization's subsidiaries in the United States and prepare reports of their operations and activities. The Board shall rely, as far as possible, on the reports of examination made by the primary federal or state supervisor of the subsidiary bank of the bank holding company or of the branch or agency of the foreign bank.

§ 225.6 Penalties for violations.

(a) *Criminal and civil penalties.* (1) Section 8 of the BHC Act provides criminal penalties for willful violation, and civil penalties for violation, by any company or individual, of the BHC Act or any regulation or order issued under it, or for making a false entry in any book, report, or statement of a bank holding company.

(2) Civil money penalty assessments for violations of the BHC Act shall be made in accordance with subpart C of the Board's Rules of Practice for Hearings (12 CFR part 263, subpart C). For any willful violation of the Bank Control Act or any regulation or order issued under it, the Board may assess a civil penalty as provided in 12 U.S.C. 1817(j)(15).

(b) *Cease-and-desist proceedings.* For any violation of the BHC Act, the Bank Control Act, this regulation, or any order or notice issued thereunder, the Board may institute a cease-and-desist proceeding in accordance with the Financial Institutions Supervisory Act of 1966, as amended (12 U.S.C. 1818(b) *et seq.*).

§ 225.7 Exceptions to tying restrictions.

(a) *Purpose.* This section establishes exceptions to the anti-tying restrictions of section 106 of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. 1971, 1972(1)). These exceptions are in addition to those in section 106. The section also restricts tying of electronic benefit transfer services by bank holding companies and their nonbank subsidiaries.

(b) *Exceptions to statute.* Subject to the limitations of paragraph (c) of this section, a bank may:

(1) *Extension to affiliates of statutory exceptions preserving traditional banking relationships.* 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 the condition or requirement that a customer:

(i) Obtain a loan, discount, deposit, or trust service from an affiliate of the bank; or

(ii) Provide to an affiliate of the bank some additional credit, property, or service that the bank could require to be provided to itself pursuant to section 106(b)(1)(C) of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. 1972(1)(C)).

(2) *Safe harbor for combined-balance discounts.* Vary the consideration for any product or package of products based on a customer's maintaining a combined minimum balance in certain products specified by the bank (eligible products), if:

(i) The bank offers deposits, and all such deposits are eligible products; and

(ii) Balances in deposits count at least as much as nondeposit products toward the minimum balance.

(3) *Safe harbor for foreign transactions.* Engage in any transaction with a customer if that customer is:

(i) A corporation, business, or other person (other than an individual) that:

(A) Is incorporated, chartered, or otherwise organized outside the United States; and

(B) Has its principal place of business outside the United States; or

(ii) An individual who is a citizen of a foreign country and is not resident in the United States.

(c) *Limitations on exceptions.* Any exception granted pursuant to this section shall terminate upon a finding by the Board that the arrangement is resulting in anti-competitive practices. The eligibility of a bank to operate under any exception granted pursuant to this section shall terminate upon a finding by the Board that its exercise of this authority is resulting in anti-competitive practices.

(d) *Extension of statute to electronic benefit transfer services.* A bank holding company or nonbank subsidiary of a bank holding company that provides electronic benefit transfer services shall be subject to the anti-tying restrictions applicable to such services set forth in section 7(i)(11) of the Food Stamp Act of 1977 (7 U.S.C. 2016(i)(11)).

(e) For purposes of this section, *bank* has the meaning given that term in section 106(a) of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. 1971), but shall also include a United States branch, agency, or commercial lending company subsidiary of a foreign bank that is subject to section 106 pursuant to section 8(d) of the International Banking Act of 1978 (12 U.S.C. 3106(d)), and any company made subject to section 106 by section 4(f)(9) or 4(h) of the BHC Act.

Subpart B—Acquisition of Bank Securities or Assets

SOURCE: Reg. Y, 62 FR 9324, Feb. 28, 1997, unless otherwise noted.

§ 225.11 Transactions requiring Board approval.

The following transactions require the Board's prior approval under section 3 of the Bank Holding Company Act except as exempted under § 225.12 or as otherwise covered by § 225.17 of this subpart:

(a) *Formation of bank holding company.* Any action that causes a bank or other company to become a bank holding company.

(b) *Acquisition of subsidiary bank.* Any action that causes a bank to become a subsidiary of a bank holding company.

(c) *Acquisition of control of bank or bank holding company securities.* (1) The acquisition by a bank holding company of direct or indirect ownership or control of any voting securities of a bank or bank holding company, if the acquisition results in the company's control of more than 5 percent of the outstanding shares of any class of voting securities of the bank or bank holding company.

(2) An acquisition includes the purchase of additional securities through the exercise of preemptive rights, but does not include securities received in a stock dividend or stock split that does not alter the bank holding company's proportional share of any class of voting securities.

(d) *Acquisition of bank assets.* The acquisition by a bank holding company or by a subsidiary thereof (other than a bank) of all or substantially all of the assets of a bank.

(e) *Merger of bank holding companies.* The merger or consolidation of bank holding companies, including a merger

through the purchase of assets and assumption of liabilities.

(f) *Transactions by foreign banking organization.* Any transaction described in paragraphs (a) through (e) of this section by a foreign banking organization that involves the acquisition of an interest in a U.S. bank or in a bank holding company for which application would be required if the foreign banking organization were a bank holding company.

§ 225.12 Transactions not requiring Board approval.

The following transactions do *not* require the Board's approval under § 225.11 of this subpart:

(a) *Acquisition of securities in fiduciary capacity.* The acquisition by a bank or other company (other than a trust that is a company) of control of voting securities of a bank or bank holding company in good faith in a fiduciary capacity, unless:

(1) The acquiring bank or other company has sole discretionary authority to vote the securities and retains this authority for more than two years; or

(2) The acquisition is for the benefit of the acquiring bank or other company, or its shareholders, employees, or subsidiaries.

(b) *Acquisition of securities in satisfaction of debts previously contracted.* The acquisition by a bank or other company of control of voting securities of a bank or bank holding company in the regular course of securing or collecting a debt previously contracted in good faith, if the acquiring bank or other company divests the securities within two years of acquisition. The Board or Reserve Bank may grant requests for up to three one-year extensions.

(c) *Acquisition of securities by bank holding company with majority control.* The acquisition by a bank holding company of additional voting securities of a bank or bank holding company if more than 50 percent of the outstanding voting securities of the bank or bank holding company is lawfully controlled by the acquiring bank holding company prior to the acquisition.

(d) *Acquisitions involving bank mergers and internal corporate reorganizations*—(1) *Transactions subject to Bank Merger Act.* The merger or consolidation of a subsidiary bank of a bank holding company with another bank, or the purchase of assets by the subsidiary bank, or a similar transaction involving subsidiary banks of a bank holding company, if the transaction requires the prior approval of a federal supervisory agency under the Bank Merger Act (12 U.S.C. 1828(c)) and does not involve the acquisition of shares of a bank. This exception does not include:

(i) The merger of a nonsubsidiary bank and a nonoperating subsidiary bank formed by a company for the purpose of acquiring the nonsubsidiary bank; or

(ii) Any transaction requiring the Board's prior approval under § 225.11(e) of this subpart.

The Board may require an application under this subpart if it determines that the merger or consolidation would have a significant adverse impact on the financial condition of the bank holding company, or otherwise requires approval under section 3 of the BHC Act.

(2) *Certain acquisitions subject to Bank Merger Act.* The acquisition by a bank holding company of shares of a bank or company controlling a bank or the merger of a company controlling a bank with the bank holding company, if the transaction is part of the merger or consolidation of the bank with a subsidiary bank (other than a nonoperating subsidiary bank) of the acquiring bank holding company, or is part of the purchase of substantially all of the assets of the bank by a subsidiary bank (other than a nonoperating subsidiary bank) of the acquiring bank holding company, and if:

(i) The bank merger, consolidation, or asset purchase occurs simultaneously with the acquisition of the shares of the bank or bank holding company or the merger of holding companies, and the bank is not operated by the acquiring bank holding company as a separate entity other than as the survivor of the merger, consolidation, or asset purchase;

(ii) The transaction requires the prior approval of a federal supervisory agency under the Bank Merger Act (12 U.S.C. 1828(c));

(iii) The transaction does not involve the acquisition of any nonbank company that would require prior approval under section 4 of the BHC Act (12 U.S.C. 1843);

(iv) Both before and after the transaction, the acquiring bank holding company meets the Board's Capital Adequacy Guidelines (Appendixes A, B, C, D, and E of this part);

(v) At least 10 days prior to the transaction, the acquiring bank holding company has provided to the Reserve Bank written notice of the transaction that contains:

(A) A copy of the filing made to the appropriate federal banking agency under the Bank Merger Act; and

(B) A description of the holding company's involvement in the transaction, the purchase price, and the source of funding for the purchase price; and

(vi) Prior to expiration of the period provided in paragraph (d)(2)(v) of this section, the Reserve Bank has not informed the bank holding company that an application under §225.11 is required.

(3) *Internal corporate reorganizations.* (i) Subject to paragraph (d)(3)(ii) of this section, any of the following transactions performed in the United States by a bank holding company:

(A) The merger of holding companies that are subsidiaries of the bank holding company;

(B) The formation of a subsidiary holding company;[1]

(C) The transfer of control or ownership of a subsidiary bank or a subsidiary holding company between one subsidiary holding company and another subsidiary holding company or the bank holding company.

(ii) A transaction described in paragraph (d)(3)(i) of this section qualifies for this exception if:

(A) The transaction represents solely a corporate reorganization involving companies and insured depository institutions that, both preceding and following the transaction, are lawfully controlled and operated by the bank holding company;

(B) The transaction does not involve the acquisition of additional voting shares of an insured depository institution that, prior to the transaction, was less than majority owned by the bank holding company;

(C) The bank holding company is not organized in mutual form; and

(D) Both before and after the transaction, the bank holding company meets the Board's Capital Adequacy Guidelines (Appendixes A, B, C, D, and E of this part).

(e) *Holding securities in escrow.* The holding of any voting securities of a bank or bank holding company in an escrow arrangement for the benefit of an applicant pending the Board's action on an application for approval of the proposed acquisition, if title to the securities and the voting rights remain with the seller and payment for the securities has not been made to the seller.

(f) *Acquisition of foreign banking organization.* The acquisition of a foreign banking organization where the foreign banking organization does not directly or indirectly own or control a bank in the United States, unless the acquisition is also by a foreign banking organization and otherwise subject to §225.11(f) of this subpart.

§225.13 Factors considered in acting on bank acquisition proposals.

(a) *Factors requiring denial.* As specified in section 3(c) of the BHC Act, the Board may not approve any application under this subpart if:

(1) The transaction would result in a monopoly or would further any combination or conspiracy to monopolize, or to attempt to monopolize, the business of banking in any part of the United States;

(2) The effect of the transaction may be substantially to lessen competition in any section of the country, tend to create a monopoly, or in any other manner be in restraint of trade, unless the Board finds that the transaction's anti-competitive effects are clearly outweighed by its probable effect in meeting the convenience and needs of the community;

(3) The applicant has failed to provide the Board with adequate assurances that it will make available such

[1] In the case of a transaction that results in the formation or designation of a new bank holding company, the new bank holding company must complete the registration requirements described in §225.5.

information on its operations or activities, and the operations or activities of any affiliate of the applicant, that the Board deems appropriate to determine and enforce compliance with the BHC Act and other applicable federal banking statutes, and any regulations thereunder; or

(4) In the case of an application involving a foreign banking organization, the foreign banking organization is not subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in its home country, as provided in § 211.24(c)(1)(ii) of the Board's Regulation K (12 CFR 211.24(c)(1)(ii)).

(b) *Other factors.* In deciding applications under this subpart, the Board also considers the following factors with respect to the applicant, its subsidiaries, any banks related to the applicant through common ownership or management, and the bank or banks to be acquired:

(1) *Financial condition.* Their financial condition and future prospects, including whether current and projected capital positions and levels of indebtedness conform to standards and policies established by the Board.

(2) *Managerial resources.* The competence, experience, and integrity of the officers, directors, and principal shareholders of the applicant, its subsidiaries, and the banks and bank holding companies concerned; their record of compliance with laws and regulations; and the record of the applicant and its affiliates of fulfilling any commitments to, and any conditions imposed by, the Board in connection with prior applications.

(3) *Convenience and needs of community.* The convenience and needs of the communities to be served, including the record of performance under the Community Reinvestment Act of 1977 (12 U.S.C. 2901 *et seq.*) and regulations issued thereunder, including the Board's Regulation BB (12 CFR part 228).

(c) *Interstate transactions.* The Board may approve any application or notice under this subpart by a bank holding company to acquire control of all or substantially all of the assets of a bank located in a state other than the home state of the bank holding company, without regard to whether the transaction is prohibited under the law of any state, if the transaction complies with the requirements of section 3(d) of the BHC Act (12 U.S.C. 1842(d)).

(d) *Conditional approvals.* The Board may impose conditions on any approval, including conditions to address competitive, financial, managerial, safety and soundness, convenience and needs, compliance or other concerns, to ensure that approval is consistent with the relevant statutory factors and other provisions of the BHC Act.

§ 225.14 Expedited action for certain bank acquisitions by well-run bank holding companies.

(a) *Filing of notice*—(1) *Information required and public notice.* As an alternative to the procedure provided in § 225.15, a bank holding company that meets the requirements of paragraph (c) of this section may satisfy the prior approval requirements of § 225.11 in connection with the acquisition of shares, assets or control of a bank, or a merger or consolidation between bank holding companies, by providing the appropriate Reserve Bank with a written notice containing the following:

(i) A certification that all of the criteria in paragraph (c) of this section are met;

(ii) A description of the transaction that includes identification of the companies and insured depository institutions involved in the transaction[2] and identification of each banking market affected by the transaction;

(iii) A description of the effect of the transaction on the convenience and needs of the communities to be served and of the actions being taken by the bank holding company to improve the

[2] If, in connection with a transaction under this subpart, any person or group of persons proposes to acquire control of the acquiring bank holding company for purposes of the Bank Control Act or § 225.41, the person or group of persons may fulfill the notice requirements of the Bank Control Act and § 225.43 by providing, as part of the submission by the acquiring bank holding company under this subpart, identifying and biographical information required in paragraph (6)(A) of the Bank Control Act (12 U.S.C. 1817(j)(6)(A)), as well as any financial or other information requested by the Reserve Bank under § 225.43.

CRA performance of any insured depository institution subsidiary that does not have at least a satisfactory CRA performance rating at the time of the transaction;

(iv) Evidence that notice of the proposal has been published in accordance with § 225.16(b)(1);

(v)(A) If the bank holding company has consolidated assets of $500 million or more, an abbreviated consolidated *pro forma* balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, consolidated *pro forma* risk-based capital ratios for the acquiring bank holding company as of the most recent quarter, and a description of the purchase price and the terms and sources of funding for the transaction;

(B) If the bank holding company has consolidated assets of less than $500 million, a *pro forma* parent-only balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, and a description of the purchase price, the terms and sources of funding for the transaction, and the sources and schedule for retiring any debt incurred in the transaction;

(vi) If the bank holding company has consolidated assets of less than $300 million, a list of and biographical information regarding any directors or senior executive officers of the resulting bank holding company that are not directors or senior executive officers of the acquiring bank holding company or of a company or institution to be acquired;

(vii) For each insured depository institution whose Tier 1 capital, total capital, total assets or risk-weighted assets change as a result of the transaction, the total risk-weighted assets, total assets, Tier 1 capital and total capital of the institution on a *pro forma* basis; and

(viii) The market indexes for each relevant banking market reflecting the *pro forma* effect of the transaction.

(2) *Waiver of unnecessary information.* The Reserve Bank may reduce the information requirements in paragraph (a)(1)(v) through (viii) of this section as appropriate.

(b)(1) *Action on proposals under this section.* The Board or the appropriate Reserve Bank shall act on a proposal submitted under this section or notify the bank holding company that the transaction is subject to the procedure in § 225.15 within 5 business days after the close of the public comment period. The Board and the Reserve Bank shall not approve any proposal under this section prior to the third business day following the close of the public comment period, unless an emergency exists that requires expedited or immediate action. The Board may extend the period for action under this section for up to 5 business days.

(2) *Acceptance of notice in event expedited procedure not available.* In the event that the Board or the Reserve Bank determines after the filing of a notice under this section that a bank holding company may not use the procedure in this section and must file an application under § 225.15, the application shall be deemed accepted for purposes of § 225.15 as of the date that the notice was filed under this section.

(c) *Criteria for use of expedited procedure.* The procedure in this section is available only if:

(1) *Well-capitalized organization*—(i) *Bank holding company.* Both at the time of and immediately after the proposed transaction, the acquiring bank holding company is well-capitalized;

(ii) *Insured depository institutions.* Both at the time of and immediately after the proposed transaction:

(A) The lead insured depository institution of the acquiring bank holding company is well-capitalized;

(B) Well-capitalized insured depository institutions control at least 80 percent of the total risk-weighted assets of insured depository institutions controlled by the acquiring bank holding company; and

(C) No insured depository institution controlled by the acquiring bank holding company is undercapitalized;

(2) *Well managed organization*—(i) *Satisfactory examination ratings.* At the time of the transaction, the acquiring bank holding company, its lead insured depository institution, and insured depository institutions that control at least 80 percent of the total risk-weighted assets of insured depository institutions controlled by the holding company are well managed and have

received at least a satisfactory rating for compliance at their most recent examination if such rating was given;

(ii) *No poorly managed institutions.* No insured depository institution controlled by the acquiring bank holding company has received 1 of the 2 lowest composite ratings at the later of the institution's most recent examination or subsequent review by the appropriate federal banking agency for the institution;

(iii) *Recently acquired institutions excluded.* Any insured depository institution that has been acquired by the bank holding company during the 12-month period preceding the date on which written notice is filed under paragraph (a) of this section may be excluded for purposes of paragraph (c)(2)(ii) of this section if :

(A) The bank holding company has developed a plan acceptable to the appropriate federal banking agency for the institution to restore the capital and management of the institution; and

(B) All insured depository institutions excluded under this paragraph represent, in the aggregate, less than 10 percent of the aggregate total risk-weighted assets of all insured depository institutions controlled by the bank holding company;

(3) *Convenience and needs criteria*—(i) *Effect on the community.* The record indicates that the proposed transaction would meet the convenience and needs of the community standard in the BHC Act; and

(ii) *Established CRA performance record.* At the time of the transaction, the lead insured depository institution of the acquiring bank holding company and insured depository institutions that control at least 80 percent of the total risk-weighted assets of insured institutions controlled by the holding company have received a satisfactory or better composite rating at the most recent examination under the Community Reinvestment Act;

(4) *Public comment.* No comment that is timely and substantive as provided in § 225.16 is received by the Board or the appropriate Reserve Bank other than a comment that supports approval of the proposal;

(5) *Competitive criteria*—(i) *Competitive screen.* Without regard to any divestitures proposed by the acquiring bank holding company, the acquisition does not cause:

(A) Insured depository institutions controlled by the acquiring bank holding company to control in excess of 35 percent of market deposits in any relevant banking market; or

(B) The Herfindahl-Hirschman index to increase by more than 200 points in any relevant banking market with a post-acquisition index of at least 1800; and

(ii) *Department of Justice.* The Department of Justice has not indicated to the Board that consummation of the transaction is likely to have a significantly adverse effect on competition in any relevant banking market;

(6) *Size of acquisition*—(i) *In general*—(A) *Limited Growth.* Except as provided in paragraph (c)(6)(ii) of this section, the sum of the aggregate risk-weighted assets to be acquired in the proposal and the aggregate risk- weighted assets acquired by the acquiring bank holding company in all other qualifying transactions does not exceed 35 percent of the consolidated risk-weighted assets of the acquiring bank holding company. For purposes of this paragraph *other qualifying transactions* means any transaction approved under this section or § 225.23 during the 12 months prior to filing the notice under this section; and

(B) *Individual size limitation.* The total risk-weighted assets to be acquired do not exceed $7.5 billion;

(ii) *Small bank holding companies.* Paragraph (c)(6)(i)(A) of this section shall not apply if, immediately following consummation of the proposed transaction, the consolidated risk-weighted assets of the acquiring bank holding company are less than $300 million;

(7) *Supervisory actions.* During the 12-month period ending on the date on which the bank holding company proposes to consummate the proposed transaction, no formal administrative order, including a written agreement, cease and desist order, capital directive, prompt corrective action directive, asset maintenance agreement, or other formal enforcement action, is or

was outstanding against the bank holding company or any insured depository institution subsidiary of the holding company, and no formal administrative enforcement proceeding involving any such enforcement action, order, or directive is or was pending;

(8) *Interstate acquisitions.* Board-approval of the transaction is not prohibited under section 3(d) of the BHC Act;

(9) *Other supervisory considerations.* Board approval of the transaction is not prohibited under the informational sufficiency or comprehensive home country supervision standards set forth in section 3(c)(3) of the BHC Act; and

(10) *Notification.* The acquiring bank holding company has not been notified by the Board, in its discretion, prior to the expiration of the period in paragraph (b)(1) of this section that an application under §225.15 is required in order to permit closer review of any financial, managerial, competitive, convenience and needs or other matter related to the factors that must be considered under this part.

(d) *Comment by primary banking supervisor*—(1) *Notice.* Upon receipt of a notice under this section, the appropriate Reserve Bank shall promptly furnish notice of the proposal and a copy of the information filed pursuant to paragraph (a) of this section to the primary banking supervisor of the insured depository institutions to be acquired.

(2) *Comment period.* The primary banking supervisor shall have 30 calendar days (or such shorter time as agreed to by the primary banking supervisor) from the date of the letter giving notice in which to submit its views and recommendations to the Board.

(3) *Action subject to supervisor's comment.* Action by the Board or the Reserve Bank on a proposal under this section is subject to the condition that the primary banking supervisor not recommend in writing to the Board disapproval of the proposal prior to the expiration of the comment period described in paragraph (d)(2) of this section. In such event, any approval given under this section shall be revoked and, if required by section 3(b) of the BHC Act, the Board shall order a hearing on the proposal.

(4) *Emergencies.* Notwithstanding paragraphs (d)(2) and (d)(3) of this section, the Board may provide the primary banking supervisor with 10 calendar days' notice of a proposal under this section if the Board finds that an emergency exists requiring expeditious action, and may act during the notice period or without providing notice to the primary banking supervisor if the Board finds that it must act immediately to prevent probable failure.

(5) *Primary banking supervisor.* For purposes of this section and §225.15(b), *the primary banking supervisor* for an institution is:

(i) The Office of the Comptroller of the Currency, in the case of a national banking association or District bank;

(ii) The appropriate supervisory authority for the State in which the bank is chartered, in the case of a State bank;

(iii) The Director of the Office of Thrift Supervision, in the case of a savings association.

(e) *Branches and agencies of foreign banking organizations.* For purposes of this section, a U.S. branch or agency of a foreign banking organization shall be considered to be an insured depository institution. A U.S. branch or agency of a foreign banking organization shall be subject to paragraph (c)(3)(ii) of this section only to the extent it is insured by the Federal Deposit Insurance Corporation in accordance with section 6 of the International Banking Act of 1978 (12 U.S.C. 3104).

[Reg. Y, 62 FR 9324, Feb. 28, 1997, as amended at 66 FR 415, Jan. 3, 2001; 71 FR 9901, Feb. 28, 2006]

§225.15 Procedures for other bank acquisition proposals.

(a) *Filing application.* Except as provided in §225.14, an application for the Board's prior approval under this subpart shall be governed by the provisions of this section and shall be filed with the appropriate Reserve Bank on the designated form.

(b) *Notice to primary banking supervisor.* Upon receipt of an application under this subpart, the Reserve Bank shall promptly furnish notice and a copy of the application to the primary banking supervisor of each bank to be acquired. The primary supervisor shall

have 30 calendar days from the date of the letter giving notice in which to submit its views and recommendations to the Board.

(c) *Accepting application for processing.* Within 7 calendar days after the Reserve Bank receives an application under this section, the Reserve Bank shall accept it for processing as of the date the application was filed or return the application if it is substantially incomplete. Upon accepting an application, the Reserve Bank shall immediately send copies to the Board. The Reserve Bank or the Board may request additional information necessary to complete the record of an application at any time after accepting the application for processing.

(d) *Action on applications*—(1) *Action under delegated authority.* The Reserve Bank shall approve an application under this section within 30 calendar days after the acceptance date for the application, unless the Reserve Bank, upon notice to the applicant, refers the application to the Board for decision because action under delegated authority is not appropriate.

(2) *Board action.* The Board shall act on an application under this subpart that is referred to it for decision within 60 calendar days after the acceptance date for the application, unless the Board notifies the applicant that the 60-day period is being extended for a specified period and states the reasons for the extension. In no event may the extension exceed the 91-day period provided in §225.16(f). The Board may, at any time, request additional information that it believes is necessary for its decision.

§ 225.16 Public notice, comments, hearings, and other provisions governing applications and notices.

(a) *In general.* The provisions of this section apply to all notices and applications filed under §225.14 and §225.15.

(b) *Public notice*—(1) *Newspaper publication*—(i) *Location of publication.* In the case of each notice or application submitted under §225.14 or §225.15, the applicant shall publish a notice in a newspaper of general circulation, in the form and at the locations specified in §262.3 of the Rules of Procedure (12 CFR 262.3);

(ii) *Contents of notice.* A newspaper notice under this paragraph shall provide an opportunity for interested persons to comment on the proposal for a period of at least 30 calendar days;

(iii) *Timing of publication.* Each newspaper notice published in connection with a proposal under this paragraph shall be published no more than 15 calendar days before and no later than 7 calendar days following the date that a notice or application is filed with the appropriate Reserve Bank.

(2) FEDERAL REGISTER *notice.* (i) *Publication by Board.* Upon receipt of a notice or application under §225.14 or §225.15, the Board shall promptly publish notice of the proposal in the FEDERAL REGISTER and shall provide an opportunity for interested persons to comment on the proposal for a period of no more than 30 days;

(ii) *Request for advance publication.* A bank holding company may request that, during the 15-day period prior to filing a notice or application under §225.14 or §225.15, the Board publish notice of a proposal in the FEDERAL REGISTER. A request for advance FEDERAL REGISTER publication shall be made in writing to the appropriate Reserve Bank and shall contain the identifying information prescribed by the Board for FEDERAL REGISTER publication;

(3) *Waiver or shortening of notice.* The Board may waive or shorten the required notice periods under this section if the Board determines that an emergency exists requiring expeditious action on the proposal, or if the Board finds that immediate action is necessary to prevent the probable failure of an insured depository institution.

(c) *Public comment*—(1) *Timely comments.* Interested persons may submit information and comments regarding a proposal filed under this subpart. A comment shall be considered timely for purposes of this subpart if the comment, together with all supplemental information, is submitted in writing in accordance with the Board's Rules of Procedure and received by the Board or the appropriate Reserve Bank prior to the expiration of the latest public comment period provided in paragraph (b) of this section.

(2) *Extension of comment period*—(i) *In general.* The Board may, in its discretion, extend the public comment period regarding any proposal submitted under this subpart.

(ii) *Requests in connection with obtaining application or notice.* In the event that an interested person has requested a copy of a notice or application submitted under this subpart, the Board may, in its discretion and based on the facts and circumstances, grant such person an extension of the comment period for up to 15 calendar days.

(iii) *Joint requests by interested person and acquiring company.* The Board will grant a joint request by an interested person and the acquiring bank holding company for an extension of the comment period for a reasonable period for a purpose related to the statutory factors the Board must consider under this subpart.

(3) *Substantive comment.* A comment will be considered substantive for purposes of this subpart unless it involves individual complaints, or raises frivolous, previously-considered or wholly unsubstantiated claims or irrelevant issues.

(d) *Notice to Attorney General.* The Board or Reserve Bank shall immediately notify the United States Attorney General of approval of any notice or application under §225.14 or §225.15.

(e) *Hearings.* As provided in section 3(b) of the BHC Act, the Board shall order a hearing on any application or notice under §225.15 if the Board receives from the primary supervisor of the bank to be acquired, within the 30-day period specified in §225.15(b), a written recommendation of disapproval of an application. The Board may order a formal or informal hearing or other proceeding on the application or notice, as provided in §262.3(i)(2) of the Board's Rules of Procedure. Any request for a hearing (other than from the primary supervisor) shall comply with §262.3(e) of the Rules of Procedure (12 CFR 262.3(e)).

(f) *Approval through failure to act*—(1) *Ninety-one day rule.* An application or notice under §225.14 or §225.15 shall be deemed approved if the Board fails to act on the application or notice within 91 calendar days after the date of submission to the Board of the complete record on the application. For this purpose, the Board acts when it issues an order stating that the Board has approved or denied the application or notice, reflecting the votes of the members of the Board, and indicating that a statement of the reasons for the decision will follow promptly.

(2) *Complete record.* For the purpose of computing the commencement of the 91-day period, the record is complete on the latest of:

(i) The date of receipt by the Board of an application or notice that has been accepted by the Reserve Bank;

(ii) The last day provided in any notice for receipt of comments and hearing requests on the application or notice;

(iii) The date of receipt by the Board of the last relevant material regarding the application or notice that is needed for the Board's decision, if the material is received from a source outside of the Federal Reserve System; or

(iv) The date of completion of any hearing or other proceeding.

(g) *Exceptions to notice and hearing requirements*—(1) *Probable bank failure.* If the Board finds it must act immediately on an application or notice in order to prevent the probable failure of a bank or bank holding company, the Board may modify or dispense with the notice and hearing requirements of this section.

(2) *Emergency.* If the Board finds that, although immediate action on an application or notice is not necessary, an emergency exists requiring expeditious action, the Board shall provide the primary supervisor 10 days to submit its recommendation. The Board may act on such an application or notice without a hearing and may modify or dispense with the other notice and hearing requirements of this section.

(h) *Waiting period.* A transaction approved under §225.14 or §225.15 shall not be consummated until 30 days after the date of approval of the application, except that a transaction may be consummated:

(1) Immediately upon approval, if the Board has determined under paragraph (g) of this section that the application or notice involves a probable bank failure;

(2) On or after the 5th calendar day following the date of approval, if the Board has determined under paragraph (g) of this section that an emergency exists requiring expeditious action; or

(3) On or after the 15th calendar day following the date of approval, if the Board has not received any adverse comments from the United States Attorney General relating to the competitive factors and the Attorney General has consented to the shorter waiting period.

§ 225.17 Notice procedure for one-bank holding company formations.

(a) *Transactions that qualify under this section.* An acquisition by a company of control of a bank may be consummated 30 days after providing notice to the appropriate Reserve Bank in accordance with paragraph (b) of this section, provided that all of the following conditions are met:

(1) The shareholder or shareholders who control at least 67 percent of the shares of the bank will control, immediately after the reorganization, at least 67 percent of the shares of the holding company in substantially the same proportion, except for changes in shareholders' interests resulting from the exercise of dissenting shareholders' rights under state or federal law;[3]

(2) No shareholder, or group of shareholders acting in concert, will, following the reorganization, own or control 10 percent or more of any class of voting shares of the bank holding company, unless that shareholder or group of shareholders was authorized, after review under the Change in Bank Control Act of 1978 (12 U.S.C. 1817(j)) by the appropriate federal banking agency for the bank, to own or control 10 percent or more of any class of voting shares of the bank;[4]

(3) The bank is adequately capitalized (as defined in section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o));

(4) The bank received at least a composite ''satisfactory'' rating at its most recent examination, in the event that the bank was examined;

(5) At the time of the reorganization, neither the bank nor any of its officers, directors, or principal shareholders is involved in any unresolved supervisory or enforcement matters with any appropriate federal banking agency;

(6) The company demonstrates that any debt that it incurs at the time of the reorganization, and the proposed means of retiring this debt, will not place undue burden on the holding company or its subsidiary on a *pro forma* basis;[5]

(7) The holding company will not, as a result of the reorganization, acquire control of any additional bank or engage in any activities other than those of managing and controlling banks; and

(8) During this period, neither the appropriate Reserve Bank nor the Board objected to the proposal or required the filing of an application under § 225.15 of this subpart.

(b) *Contents of notice.* A notice filed under this paragraph shall include:

(1) Certification by the notificant's board of directors that the requirements of 12 U.S.C. 1842(a)(C) and this section are met by the proposal;

(2) A list identifying all principal shareholders of the bank prior to the reorganization and of the holding company following the reorganization, and specifying the percentage of shares held by each principal shareholder in the bank and proposed to be held in the new holding company;

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[3] A shareholder of a bank in reorganization will be considered to have the same proportional interest in the holding company if the shareholder interest increases, on a *pro rata* basis, as a result of either the redemption of shares from dissenting shareholders by the bank or bank holding company, or the acquisition of shares of dissenting shareholders by the remaining shareholders.

[4] This procedure is not available in cases in which the exercise of dissenting shareholders' rights would cause a company that is not a bank holding company (other than the company in formation) to be required to register as a bank holding company. This procedure also is not available for the formation of a bank holding company organized in mutual form.

[5] For a banking organization with consolidated assets, on a *pro forma* basis, of less than $500 million (other than a banking organization that will control a de novo bank), this requirement is satisfied if the proposal complies with the Board's Small Bank Holding Company Policy Statement (Appendix C of this part).

(3) A description of the resulting management of the proposed bank holding company and its subsidiary bank, including:

(i) Biographical information regarding any senior officers and directors of the resulting bank holding company who were not senior officers or directors of the bank prior to the reorganization; and

(ii) A detailed history of the involvement of any officer, director, or principal shareholder of the resulting bank holding company in any administrative or criminal proceeding; and

(4) *Pro forma* financial statements for the holding company, and a description of the amount, source, and terms of debt, if any, that the bank holding company proposes to incur, and information regarding the sources and timing for debt service and retirement.

(c) *Acknowledgment of notice.* Within 7 calendar days following receipt of a notice under this section, the Reserve Bank shall provide the notificant with a written acknowledgment of receipt of the notice. This written acknowledgment shall indicate that the transaction described in the notice may be consummated on the 30th calendar day after the date of receipt of the notice if the Reserve Bank or the Board has not objected to the proposal during that time.

(d) *Application required upon objection.* The Reserve Bank or the Board may object to a proposal during the notice period by providing the bank holding company with a written explanation of the reasons for the objection. In such case, the bank holding company may file an application for prior approval of the proposal pursuant to § 225.15 of this subpart.

[Reg. Y, 62 FR 9319, Feb. 28, 1997, as amended at 71 FR 9902, Feb. 28, 2006]

Subpart C—Nonbanking Activities and Acquisitions by Bank Holding Companies

SOURCE: Reg. Y, 62 FR 9329, Feb. 28, 1997, unless otherwise noted.

§ 225.21 Prohibited nonbanking activities and acquisitions; exempt bank holding companies.

(a) *Prohibited nonbanking activities and acquisitions.* Except as provided in § 225.22 of this subpart, a bank holding company or a subsidiary may not engage in, or acquire or control, directly or indirectly, voting securities or assets of a company engaged in, any activity other than:

(1) Banking or managing or controlling banks and other subsidiaries authorized under the BHC Act; and

(2) An activity that the Board determines to be so closely related to banking, or managing or controlling banks as to be a proper incident thereto, including any incidental activities that are necessary to carry on such an activity, if the bank holding company has obtained the prior approval of the Board for that activity in accordance with the requirements of this regulation.

(b) *Exempt bank holding companies.* The following bank holding companies are exempt from the provisions of this subpart:

(1) *Family-owned companies.* Any company that is a ''company covered in 1970'' (as defined in section 2(b) of the BHC Act), more than 85 percent of the voting securities of which was collectively owned on June 30, 1968, and continuously thereafter, by members of the same family (or their spouses) who are lineal descendants of common ancestors.

(2) *Labor, agricultural, and horticultural organizations.* Any company that was on January 4, 1977, both a bank holding company and a labor, agricultural, or horticultural organization exempt from taxation under section 501 of the Internal Revenue Code (26 U.S.C. 501(c)).

(3) *Companies granted hardship exemption.* Any bank holding company that has controlled only one bank since before July 1, 1968, and that has been granted an exemption by the Board under section 4(d) of the BHC Act, subject to any conditions imposed by the Board.

(4) *Companies granted exemption on other grounds.* Any company that acquired control of a bank before December 10, 1982, without the Board's prior

approval under section 3 of the BHC Act, on the basis of a narrow interpretation of the term *demand deposit* or *commercial loan*, if the Board has determined that:

(i) Coverage of the company as a bank holding company under this subpart would be unfair or represent an unreasonable hardship; and

(ii) Exclusion of the company from coverage under this part is consistent with the purposes of the BHC Act and section 106 of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. 1971, 1972(1)). The provisions of § 225.4 of subpart A of this part do not apply to a company exempt under this paragraph.

§ 225.22 Exempt nonbanking activities and acquisitions.

(a) *Certain de novo activities.* A bank holding company may, either directly or indirectly, engage *de novo* in any nonbanking activity listed in § 225.28(b) (other than operation of an insured depository institution) without obtaining the Board's prior approval if the bank holding company:

(1) Meets the requirements of paragraphs (c) (1), (2), and (6) of § 225.23;

(2) Conducts the activity in compliance with all Board orders and regulations governing the activity; and

(3) Within 10 business days after commencing the activity, provides written notice to the appropriate Reserve Bank describing the activity, identifying the company or companies engaged in the activity, and certifying that the activity will be conducted in accordance with the Board's orders and regulations and that the bank holding company meets the requirements of paragraphs (c) (1), (2), and (6) of § 225.23.

(b) *Servicing activities.* A bank holding company may, without the Board's prior approval under this subpart, furnish services to or perform services for, or establish or acquire a company that engages solely in servicing activities for:

(1) The bank holding company or its subsidiaries in connection with their activities as authorized by law, including services that are necessary to fulfill commitments entered into by the subsidiaries with third parties, if the bank holding company or servicing company complies with the Board's published interpretations and does not act as principal in dealing with third parties; and

(2) The internal operations of the bank holding company or its subsidiaries. Services for the internal operations of the bank holding company or its subsidiaries include, but are not limited to:

(i) Accounting, auditing, and appraising;

(ii) Advertising and public relations;

(iii) Data processing and data transmission services, data bases, or facilities;

(iv) Personnel services;

(v) Courier services;

(vi) Holding or operating property used wholly or substantially by a subsidiary in its operations or for its future use;

(vii) Liquidating property acquired from a subsidiary;

(viii) Liquidating property acquired from any sources either prior to May 9, 1956, or the date on which the company became a bank holding company, whichever is later; and

(ix) Selling, purchasing, or underwriting insurance, such as blanket bond insurance, group insurance for employees, and property and casualty insurance.

(c) *Safe deposit business.* A bank holding company or nonbank subsidiary may, without the Board's prior approval, conduct a safe deposit business, or acquire voting securities of a company that conducts such a business.

(d) *Nonbanking acquisitions not requiring prior Board approval.* The Board's prior approval is not required under this subpart for the following acquisitions:

(1) *DPC acquisitions.* (i) Voting securities or assets, acquired by foreclosure or otherwise, in the ordinary course of collecting a debt previously contracted (DPC property) in good faith, if the DPC property is divested within two years of acquisition.

(ii) The Board may, upon request, extend this two-year period for up to three additional years. The Board may permit additional extensions for up to 5 years (for a total of 10 years), for shares, real estate or other assets

where the holding company demonstrates that each extension would not be detrimental to the public interest and either the bank holding company has made good faith attempts to dispose of such shares, real estate or other assets or disposal of the shares, real estate or other assets during the initial period would have been detrimental to the company.

(iii) Transfers of DPC property within the bank holding company system do not extend any period for divestiture of the property.

(2) *Securities or assets required to be divested by subsidiary.* Voting securities or assets required to be divested by a subsidiary at the request of an examining federal or state authority (except by the Board under the BHC Act or this regulation), if the bank holding company divests the securities or assets within two years from the date acquired from the subsidiary.

(3) *Fiduciary investments.* Voting securities or assets acquired by a bank or other company (other than a trust that is a company) in good faith in a fiduciary capacity, if the voting securities or assets are:

(i) Held in the ordinary course of business; and

(ii) Not acquired for the benefit of the company or its shareholders, employees, or subsidiaries.

(4) *Securities eligible for investment by national bank.* Voting securities of the kinds and amounts explicitly eligible by federal statute (other than section 4 of the Bank Service Corporation Act, 12 U.S.C. 1864) for investment by a national bank, and voting securities acquired prior to June 30, 1971, in reliance on section 4(c)(5) of the BHC Act and interpretations of the Comptroller of the Currency under section 5136 of the Revised Statutes (12 U.S.C. 24(7)).

(5) *Securities or property representing 5 percent or less of a company.* Voting securities of a company or property that, in the aggregate, represent 5 percent or less of the outstanding shares of any class of voting securities of a company, or that represent a 5 percent interest or less in the property, subject to the provisions of 12 CFR 225.137.

(6) *Securities of investment company.* Voting securities of an investment company that is solely engaged in investing in securities and that does not own or control more than 5 percent of the outstanding shares of any class of voting securities of any company.

(7) *Assets acquired in ordinary course of business.* Assets of a company acquired in the ordinary course of business, subject to the provisions of 12 CFR 225.132, if the assets relate to activities in which the acquiring company has previously received Board approval under this regulation to engage.

(8) *Asset acquisitions by lending company or industrial bank.* Assets of an office(s) of a company, all or substantially all of which relate to making, acquiring, or servicing loans if:

(i) The acquiring company has previously received Board approval under this regulation or is not required to obtain prior Board approval under this regulation to engage in lending activities or industrial banking activities;

(ii) The assets acquired during any 12-month period do not represent more than 50 percent of the risk-weighted assets (on a consolidated basis) of the acquiring lending company or industrial bank, or more than $100 million, whichever amount is less;

(iii) The assets acquired do not represent more than 50 percent of the selling company's consolidated assets that are devoted to lending activities or industrial banking business;

(iv) The acquiring company notifies the Reserve Bank of the acquisition within 30 days after the acquisition; and

(v) The acquiring company, after giving effect to the transaction, meets the Board's Capital Adequacy Guidelines (Appendix A of this part), and the Board has not previously notified the acquiring company that it may not acquire assets under the exemption in this paragraph.

(e) *Acquisition of securities by subsidiary banks*—(1) *National bank.* A national bank or its subsidiary may, without the Board's approval under this subpart, acquire or retain securities on the basis of section 4(c)(5) of the BHC Act in accordance with the regulations of the Comptroller of the Currency.

(2) *State bank.* A state-chartered bank or its subsidiary may, insofar as federal law is concerned, and without the

Board's prior approval under this subpart:

(i) Acquire or retain securities, on the basis of section 4(c)(5) of the BHC Act, of the kinds and amounts explicitly eligible by federal statute for investment by a national bank; or

(ii) Acquire or retain all (but, except for directors' qualifying shares, not less than all) of the securities of a company that engages solely in activities in which the parent bank may engage, at locations at which the bank may engage in the activity, and subject to the same limitations as if the bank were engaging in the activity directly.

(f) *Activities and securities of new bank holding companies.* A company that becomes a bank holding company may, for a period of two years, engage in nonbanking activities and control voting securities or assets of a nonbank subsidiary, if the bank holding company engaged in such activities or controlled such voting securities or assets on the date it became a bank holding company. The Board may grant requests for up to three one-year extensions of the two-year period.

(g) *Grandfathered activities and securities.* Unless the Board orders divestiture or termination under section 4(a)(2) of the BHC Act, a ''company covered in 1970,'' as defined in section 2(b) of the BHC Act, may:

(1) Retain voting securities or assets and engage in activities that it has lawfully held or engaged in continuously since June 30, 1968; and

(2) Acquire voting securities of any newly formed company to engage in such activities.

(h) *Securities or activities exempt under Regulation K.* A bank holding company may acquire voting securities or assets and engage in activities as authorized in Regulation K (12 CFR part 211).

§ 225.23 Expedited action for certain nonbanking proposals by well-run bank holding companies.

(a) *Filing of notice*—(1) *Information required.* A bank holding company that meets the requirements of paragraph (c) of this section may satisfy the notice requirement of this subpart in connection with the acquisition of voting securities or assets of a company engaged in nonbanking activities that the Board has permitted by order or regulation (other than an insured depository institution),[1] or a proposal to engage *de novo,* either directly or indirectly, in a nonbanking activity that the Board has permitted by order or by regulation, by providing the appropriate Reserve Bank with a written notice containing the following:

(i) A certification that all of the criteria in paragraph (c) of this section are met;

(ii) A description of the transaction that includes identification of the companies involved in the transaction, the activities to be conducted, and a commitment to conduct the proposed activities in conformity with the Board's regulations and orders governing the conduct of the proposed activity;

(iii) If the proposal involves an acquisition of a going concern:

(A) If the bank holding company has consolidated assets of $500 million or more, an abbreviated consolidated *pro forma* balance sheet for the acquiring bank holding company as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, consolidated *pro forma* risk-based capital ratios for the acquiring bank holding company as of the most recent quarter, a description of the purchase price and the terms and sources of funding for the transaction, and the total revenue and net income of the company to be acquired;

(B) If the bank holding company has consolidated assets of less than $500 million, a *pro forma* parent-only balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, a description of the purchase price and the terms and sources of funding for the transaction and the sources and schedule for retiring any debt incurred in the transaction, and the total assets, off-balance sheet

[1] A bank holding company may acquire voting securities or assets of a savings association or other insured depository institution that is not a bank by using the procedures in § 225.14 of subpart B if the bank holding company and the proposal qualify under that section as if the savings association or other institution were a bank for purposes of that section.

items, revenue and net income of the company to be acquired;

(C) For each insured depository institution whose Tier 1 capital, total capital, total assets or risk-weighted assets change as a result of the transaction, the total risk-weighted assets, total assets, Tier 1 capital and total capital of the institution on a *pro forma* basis;

(iv) Identification of the geographic markets in which competition would be affected by the proposal, a description of the effect of the proposal on competition in the relevant markets, a list of the major competitors in that market in the proposed activity if the affected market is local in nature, and, if requested, the market indexes for the relevant market; and

(v) A description of the public benefits that can reasonably be expected to result from the transaction.

(2) *Waiver of unnecessary information.* The Reserve Bank may reduce the information requirements in paragraphs (a)(1) (iii) and (iv) of this section as appropriate.

(b)(1) *Action on proposals under this section.* The Board or the appropriate Reserve Bank shall act on a proposal submitted under this section, or notify the bank holding company that the transaction is subject to the procedure in §225.24, within 12 business days following the filing of all of the information required in paragraph (a) of this section.

(2) *Acceptance of notice if expedited procedure not available.* If the Board or the Reserve Bank determines, after the filing of a notice under this section, that a bank holding company may not use the procedure in this section and must file a notice under §225.24, the notice shall be deemed accepted for purposes of §225.24 as of the date that the notice was filed under this section.

(c) *Criteria for use of expedited procedure.* The procedure in this section is available only if:

(1) *Well-capitalized organization*—(i) *Bank holding company.* Both at the time of and immediately after the proposed transaction, the acquiring bank holding company is well-capitalized;

(ii) *Insured depository institutions.* Both at the time of and immediately after the transaction:

(A) The lead insured depository institution of the acquiring bank holding company is well-capitalized;

(B) Well-capitalized insured depository institutions control at least 80 percent of the total risk-weighted assets of insured depository institutions controlled by the acquiring bank holding company; and

(C) No insured depository institution controlled by the acquiring bank holding company is undercapitalized;

(2) *Well managed organization*—(i) *Satisfactory examination ratings.* At the time of the transaction, the acquiring bank holding company, its lead insured depository institution, and insured depository institutions that control at least 80 percent of the total risk-weighted assets of insured depository institutions controlled by the holding company are well managed and have received at least a satisfactory rating for compliance at their most recent examination if such rating was given;

(ii) *No poorly managed institutions.* No insured depository institution controlled by the acquiring bank holding company has received 1 of the 2 lowest composite ratings at the later of the institution's most recent examination or subsequent review by the appropriate federal banking agency for the institution.

(iii) *Recently acquired institutions excluded.* Any insured depository institution that has been acquired by the bank holding company during the 12-month period preceding the date on which written notice is filed under paragraph (a) of this section may be excluded for purposes of paragraph (c)(2)(ii) of this section if:

(A) The bank holding company has developed a plan acceptable to the appropriate federal banking agency for the institution to restore the capital and management of the institution; and

(B) All insured depository institutions excluded under this paragraph represent, in the aggregate, less than 10 percent of the aggregate total risk-weighted assets of all insured depository institutions controlled by the bank holding company;

(3) *Permissible activity.* (i) The Board has determined by regulation or order

that each activity proposed to be conducted is so closely related to banking, or managing or controlling banks, as to be a proper incident thereto; and

(ii) The Board has not indicated that proposals to engage in the activity are subject to the notice procedure provided in § 225.24;

(4) *Competitive criteria*—(i) *Competitive screen.* In the case of the acquisition of a going concern, the acquisition, without regard to any divestitures proposed by the acquiring bank holding company, does not cause:

(A) The acquiring bank holding company to control in excess of 35 percent of the market share in any relevant market; or

(B) The Herfindahl-Hirschman index to increase by more than 200 points in any relevant market with a post-acquisition index of at least 1800; and

(ii) *Other competitive factors.* The Board has not indicated that the transaction is subject to close scrutiny on competitive grounds;

(5) *Size of acquisition*—(i) *In general*—(A) *Limited growth.* Except as provided in paragraph (c)(5)(ii) of this section, the sum of aggregate risk-weighted assets to be acquired in the proposal and the aggregate risk-weighted assets acquired by the acquiring bank holding company in all other qualifying transactions does not exceed 35 percent of the consolidated risk-weighted assets of the acquiring bank holding company. For purposes of this paragraph, ''other qualifying transactions'' means any transaction approved under this section or § 225.14 during the 12 months prior to filing the notice under this section;

(B) *Consideration paid.* The gross consideration to be paid by the acquiring bank holding company in the proposal does not exceed 15 percent of the consolidated Tier 1 capital of the acquiring bank holding company; and

(C) *Individual size limitation.* The total risk-weighted assets to be acquired do not exceed $7.5 billion;

(ii) *Small bank holding companies.* Paragraph (c)(5)(i)(A) of this section shall not apply if, immediately following consummation of the proposed transaction, the consolidated risk-weighted assets of the acquiring bank holding company are less than $300 million;

(6) *Supervisory actions.* During the 12-month period ending on the date on which the bank holding company proposes to consummate the proposed transaction, no formal administrative order, including a written agreement, cease and desist order, capital directive, prompt corrective action directive, asset maintenance agreement, or other formal enforcement order is or was outstanding against the bank holding company or any insured depository institution subsidiary of the holding company, and no formal administrative enforcement proceeding involving any such enforcement action, order, or directive is or was pending; and

(7) *Notification.* The bank holding company has not been notified by the Board, in its discretion, prior to the expiration of the period in paragraph (b) of this section that a notice under § 225.24 is required in order to permit closer review of any potential adverse effect or other matter related to the factors that must be considered under this part.

(d) *Branches and agencies of foreign banking organizations.* For purposes of this section, a U.S. branch or agency of a foreign banking organization shall be considered to be an insured depository institution.

[Reg. Y, 62 FR 9329, Feb. 28, 1997, as amended at 66 FR 415, Jan. 3, 2001; 71 FR 9902, Feb. 28, 2006]

§ 225.24 Procedures for other nonbanking proposals.

(a) *Notice required for nonbanking activities.* Except as provided in § 225.22 and § 225.23, a notice for the Board's prior approval under § 225.21(a) to engage in or acquire a company engaged in a nonbanking activity shall be filed by a bank holding company (including a company seeking to become a bank holding company) with the appropriate Reserve Bank in accordance with this section and the Board's Rules of Procedure (12 CFR 262.3).

(1) *Engaging de novo in listed activities.* A bank holding company seeking to commence or to engage *de novo,* either directly or through a subsidiary, in a nonbanking activity listed in § 225.28

shall file a notice containing a description of the activities to be conducted and the identity of the company that will conduct the activity.

(2) *Acquiring company engaged in listed activities.* A bank holding company seeking to acquire or control voting securities or assets of a company engaged in a nonbanking activity listed in §225.28 shall file a notice containing the following:

(i) A description of the proposal, including a description of each proposed activity, and the effect of the proposal on competition among entities engaging in each proposed activity in each relevant market with relevant market indexes;

(ii) The identity of any entity involved in the proposal, and, if the notificant proposes to conduct the activity through an existing subsidiary, a description of the existing activities of the subsidiary;

(iii) A statement of the public benefits that can reasonably be expected to result from the proposal;

(iv) If the bank holding company has consolidated assets of $150 million or more:

(A) Parent company and consolidated *pro forma* balance sheets for the acquiring bank holding company as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction;

(B) Consolidated *pro forma* risk-based capital and leverage ratio calculations for the acquiring bank holding company as of the most recent quarter; and

(C) A description of the purchase price and the terms and sources of funding for the transaction;

(v) If the bank holding company has consolidated assets of less than $150 million:

(A) A *pro forma* parent-only balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction; and

(B) A description of the purchase price and the terms and sources of funding for the transaction and, if the transaction is debt funded, one-year income statement and cash flow projections for the parent company, and the sources and schedule for retiring any debt incurred in the transaction;

(vi) For each insured depository institution whose Tier 1 capital, total capital, total assets or risk-weighted assets change as a result of the transaction, the total risk-weighted assets, total assets, Tier 1 capital and total capital of the institution on a *pro forma* basis; and

(vii) A description of the management expertise, internal controls and risk management systems that will be utilized in the conduct of the proposed activities; and

(viii) A copy of the purchase agreements, and balance sheet and income statements for the most recent quarter and year-end for any company to be acquired.

(b) *Notice provided to Board.* The Reserve Bank shall immediately send to the Board a copy of any notice received under paragraphs (a)(2) or (a)(3) of this section.

(c) *Notice to public*—(1) *Listed activities and activities approved by order*—(i) In a case involving an activity listed in §225.28 or previously approved by the Board by order, the Reserve Bank shall notify the Board for publication in the FEDERAL REGISTER immediately upon receipt by the Reserve Bank of:

(A) A notice under this section; or

(B) A written request that notice of a proposal under this section or §225.23 be published in the FEDERAL REGISTER. Such a request may request that FEDERAL REGISTER publication occur up to 15 calendar days prior to submission of a notice under this subpart.

(ii) The FEDERAL REGISTER notice published under this paragraph shall invite public comment on the proposal, generally for a period of 15 days.

(2) *New activities*—(i) *In general.* In the case of a notice under this subpart involving an activity that is not listed in §225.28 and that has not been previously approved by the Board by order, the Board shall send notice of the proposal to the FEDERAL REGISTER for publication, unless the Board determines that the notificant has not demonstrated that the activity is so closely related to banking or to managing or controlling banks as to be a proper incident thereto. The FEDERAL REGISTER notice shall invite public comment on the proposal for a reasonable period of time, generally for 30 days.

(ii) *Time for publication.* The Board shall send the notice required under this paragraph to the FEDERAL REGISTER within 10 business days of acceptance by the Reserve Bank. The Board may extend the 10-day period for an additional 30 calendar days upon notice to the notificant. In the event notice of a proposal is not published for comment, the Board shall inform the notificant of the reasons for the decision.

(d) *Action on notices*—(1) *Reserve Bank action*—(i) *In general.* Within 30 calendar days after receipt by the Reserve Bank of a notice filed pursuant to paragraphs (a)(1) or (a)(2) of this section, the Reserve Banks shall:

(A) Approve the notice; or

(B) Refer the notice to the Board for decision because action under delegated authority is not appropriate.

(ii) *Return of incomplete notice.* Within 7 calendar days of receipt, the Reserve Bank may return any notice as informationally incomplete that does not contain all of the information required by this subpart. The return of such a notice shall be deemed action on the notice.

(iii) *Notice of action.* The Reserve Bank shall promptly notify the bank holding company of any action or referral under this paragraph.

(iv) *Close of public comment period.* The Reserve Bank shall not approve any notice under this paragraph (d)(1) of this section prior to the third business day after the close of the public comment period, unless an emergency exists that requires expedited or immediate action.

(2) *Board action; internal schedule.* The Board seeks to act on every notice referred to it for decision within 60 days of the date that the notice is filed with the Reserve Bank. If the Board is unable to act within this period, the Board shall notify the notificant and explain the reasons and the date by which the Board expects to act.

(3)(i) *Required time limit for System action.* The Board or the Reserve Bank shall act on any notice under this section within 60 days after the submission of a complete notice.

(ii) *Extension of required period for action* (A) *In general.*—The Board may extend the 60-day period required for Board action under paragraph (d)(3)(i) of this section for an additional 30 days upon notice to the notificant.

(B) *Unlisted activities.* If a notice involves a proposal to engage in an activity that is not listed in § 225.28, the Board may extend the period required for Board action under paragraph (d)(3)(i) of this section for an additional 90 days. This 90-day extension is in addition to the 30-day extension period provided in paragraph (d)(3)(ii)(A) of this section. The Board shall notify the notificant that the notice period has been extended and explain the reasons for the extension.

(4) *Requests for additional information.* The Board or the Reserve Bank may modify the information requirements under this section or at any time request any additional information that either believes is needed for a decision on any notice under this section.

(5) *Tolling of period.* The Board or the Reserve Bank may at any time extend or toll the time period for action on a notice for any period with the consent of the notificant.

[Reg. Y, 62 FR 9332, Feb. 28, 1997, as amended at 62 FR 60640, Nov. 12, 1997; 65 FR 14438, Mar. 17, 2000]

§ 225.25 Hearings, alteration of activities, and other matters.

(a) *Hearings*—(1) *Procedure to request hearing.* Any request for a hearing on a notice under this subpart shall comply with the provisions of 12 CFR 262.3(e).

(2) *Determination to hold hearing.* The Board may order a formal or informal hearing or other proceeding on a notice as provided in 12 CFR 262.3(i)(2). The Board shall order a hearing only if there are disputed issues of material fact that cannot be resolved in some other manner.

(3) *Extension of period for hearing.* The Board may extend the time for action on any notice for such time as is reasonably necessary to conduct a hearing and evaluate the hearing record. Such extension shall not exceed 91 calendar days after the date of submission to the Board of the complete record on the notice. The procedures for computation of the 91-day rule as set forth in § 225.16(f) apply to notices under this subpart that involve hearings.

(b) *Approval through failure to act.* (1) Except as provided in paragraph (a) of this section or §225.24(d)(5), a notice under this subpart shall be deemed to be approved at the conclusion of the period that begins on the date the complete notice is received by the Reserve Bank or the Board and that ends 60 calendar days plus any applicable extension and tolling period thereafter.

(2) *Complete notice.* For purposes of paragraph (b)(1) of this section, a notice shall be deemed complete at such time as it contains all information required by this subpart and all other information requested by the Board or the Reserve Bank.

(c) *Notice to expand or alter nonbanking activities*—(1) *De novo expansion.* A notice under this subpart is required to open a new office or to form a subsidiary to engage in, or to relocate an existing office engaged in, a nonbanking activity that the Board has previously approved for the bank holding company under this regulation, only if:

(i) The Board's prior approval was limited geographically;

(ii) The activity is to be conducted in a country outside of the United States and the bank holding company has not previously received prior Board approval under this regulation to engage in the activity in that country; or

(iii) The Board or appropriate Reserve Bank has notified the company that a notice under this subpart is required.

(2) *Activities outside United States.* With respect to activities to be engaged in outside the United States that require approval under this subpart, the procedures of this section apply only to activities to be engaged in directly by a bank holding company that is not a qualifying foreign banking organization, or by a nonbank subsidiary of a bank holding company approved under this subpart. Regulation K (12 CFR part 211) governs other international operations of bank holding companies.

(3) *Alteration of nonbanking activity.* Unless otherwise permitted by the Board, a notice under this subpart is required to alter a nonbanking activity in any material respect from that considered by the Board in acting on the application or notice to engage in the activity.

(d) *Emergency savings association acquisitions.* In the case of a notice to acquire a savings association, the Board may modify or dispense with the public notice and hearing requirements of this subpart if the Board finds that an emergency exists that requires the Board to act immediately and the primary federal regulator of the institution concurs.

[Reg. Y, 62 FR 9333, Feb. 28, 1997, as amended by Reg. Y, 62 FR 60640, Nov. 12, 1997]

§225.26 Factors considered in acting on nonbanking proposals.

(a) *In general.* In evaluating a notice under §225.23 or §225.24, the Board shall consider whether the notificant's performance of the activities can reasonably be expected to produce benefits to the public (such as greater convenience, increased competition, and gains in efficiency) that outweigh possible adverse effects (such as undue concentration of resources, decreased or unfair competition, conflicts of interest, and unsound banking practices).

(b) *Financial and managerial resources.* Consideration of the factors in paragraph (a) of this section includes an evaluation of the financial and managerial resources of the notificant, including its subsidiaries and any company to be acquired, the effect of the proposed transaction on those resources, and the management expertise, internal control and risk-management systems, and capital of the entity conducting the activity.

(c) *Competitive effect of de novo proposals.* Unless the record demonstrates otherwise, the commencement or expansion of a nonbanking activity *de novo* is presumed to result in benefits to the public through increased competition.

(d) *Denial for lack of information.* The Board may deny any notice submitted under this subpart if the notificant neglects, fails, or refuses to furnish all information required by the Board.

(e) *Conditional approvals.* The Board may impose conditions on any approval, including conditions to address permissibility, financial, managerial, safety and soundness, competitive, compliance, conflicts of interest, or

other concerns to ensure that approval is consistent with the relevant statutory factors and other provisions of the BHC Act.

§ 225.27 Procedures for determining scope of nonbanking activities.

(a) *Advisory opinions regarding scope of previously approved nonbanking activities*—(1) *Request for advisory opinion.* Any person may submit a request to the Board for an advisory opinion regarding the scope of any permissible nonbanking activity. The request shall be submitted in writing to the Board and shall identify the proposed parameters of the activity, or describe the service or product that will be provided, and contain an explanation supporting an interpretation regarding the scope of the permissible nonbanking activity.

(2) *Response to request.* The Board shall provide an advisory opinion within 45 days of receiving a written request under this paragraph.

(b) *Procedure for consideration of new activities*—(1) *Initiation of proceeding.* The Board may, at any time, on its own initiative or in response to a written request from any person, initiate a proceeding to determine whether any activity is so closely related to banking or managing or controlling banks as to be a proper incident thereto.

(2) *Requests for determination.* Any request for a Board determination that an activity is so closely related to banking or managing or controlling banks as to be a proper incident thereto, shall be submitted to the Board in writing, and shall contain evidence that the proposed activity is so closely related to banking or managing or controlling banks as to be a proper incident thereto.

(3) *Publication.* The Board shall publish in the FEDERAL REGISTER notice that it is considering the permissibility of a new activity and invite public comment for a period of at least 30 calendar days. In the case of a request submitted under paragraph (b) of this section, the Board may determine not to publish notice of the request if the Board determines that the requester has provided no reasonable basis for a determination that the activity is so closely related to banking, or managing or controlling banks as to be a proper incident thereto, and notifies the requester of the determination.

(4) *Comments and hearing requests.* Any comment and any request for a hearing regarding a proposal under this section shall comply with the provisions of § 262.3(e) of the Board's Rules of Procedure (12 CFR 262.3(e)).

§ 225.28 List of permissible nonbanking activities.

(a) *Closely related nonbanking activities.* The activities listed in paragraph (b) of this section are so closely related to banking or managing or controlling banks as to be a proper incident thereto, and may be engaged in by a bank holding company or its subsidiary in accordance with the requirements of this regulation.

(b) *Activities determined by regulation to be permissible*—(1) *Extending credit and servicing loans.* Making, acquiring, brokering, or servicing loans or other extensions of credit (including factoring, issuing letters of credit and accepting drafts) for the company's account or for the account of others.

(2) *Activities related to extending credit.* Any activity usual in connection with making, acquiring, brokering or servicing loans or other extensions of credit, as determined by the Board. The Board has determined that the following activities are usual in connection with making, acquiring, brokering or servicing loans or other extensions of credit:

(i) *Real estate and personal property appraising.* Performing appraisals of real estate and tangible and intangible personal property, including securities.

(ii) *Arranging commercial real estate equity financing.* Acting as intermediary for the financing of commercial or industrial income-producing real estate by arranging for the transfer of the title, control, and risk of such a real estate project to one or more investors, if the bank holding company and its affiliates do not have an interest in, or participate in managing or developing, a real estate project for which it arranges equity financing, and do not promote or sponsor the development of the property.

(iii) *Check-guaranty services.* Authorizing a subscribing merchant to accept

personal checks tendered by the merchant's customers in payment for goods and services, and purchasing from the merchant validly authorized checks that are subsequently dishonored.

(iv) *Collection agency services.* Collecting overdue accounts receivable, either retail or commercial.

(v) *Credit bureau services.* Maintaining information related to the credit history of consumers and providing the information to a credit grantor who is considering a borrower's application for credit or who has extended credit to the borrower.

(vi) *Asset management, servicing, and collection activities.* Engaging under contract with a third party in asset management, servicing, and collection[2] of assets of a type that an insured depository institution may originate and own, if the company does not engage in real property management or real estate brokerage services as part of these services.

(vii) *Acquiring debt in default.* Acquiring debt that is in default at the time of acquisition, if the company:

(A) Divests shares or assets securing debt in default that are not permissible investments for bank holding companies, within the time period required for divestiture of property acquired in satisfaction of a debt previously contracted under § 225.12(b);[3]

(B) Stands only in the position of a creditor and does not purchase equity of obligors of debt in default (other than equity that may be collateral for such debt); and

(C) Does not acquire debt in default secured by shares of a bank or bank holding company.

(viii) *Real estate settlement servicing.* Providing real estate settlement services.[4]

(3) *Leasing personal or real property.* Leasing personal or real property or acting as agent, broker, or adviser in leasing such property if:

(i) The lease is on a nonoperating basis;[5]

(ii) The initial term of the lease is at least 90 days;

(iii) In the case of leases involving real property:

(A) At the inception of the initial lease, the effect of the transaction will yield a return that will compensate the lessor for not less than the lessor's full investment in the property plus the estimated total cost of financing the property over the term of the lease from rental payments, estimated tax benefits, and the estimated residual value of the property at the expiration of the initial lease; and

(B) The estimated residual value of property for purposes of paragraph (b)(3)(iii)(A) of this section shall not exceed 25 percent of the acquisition cost of the property to the lessor.

(4) *Operating nonbank depository institutions*—(i) *Industrial banking.* Owning, controlling, or operating an industrial bank, Morris Plan bank, or industrial loan company, so long as the institution is not a bank.

(ii) *Operating savings association.* Owning, controlling, or operating a savings association, if the savings association engages only in deposit-taking activities, lending, and other activities that

[2] Asset management services include acting as agent in the liquidation or sale of loans and collateral for loans, including real estate and other assets acquired through foreclosure or in satisfaction of debts previously contracted.

[3] For this purpose, the divestiture period for property begins on the date that the debt is acquired, regardless of when legal title to the property is acquired.

[4] For purposes of this section, real estate settlement services do not include providing title insurance as principal, agent, or broker.

[5] The requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly, engage in operating, servicing, maintaining, or repairing leased property during the lease term. For purposes of the leasing of automobiles, the requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly: (1) Provide servicing, repair, or maintenance of the leased vehicle during the lease term; (2) purchase parts and accessories in bulk or for an individual vehicle after the lessee has taken delivery of the vehicle; (3) provide the loan of an automobile during servicing of the leased vehicle; (4) purchase insurance for the lessee; or (5) provide for the renewal of the vehicle's license merely as a service to the lessee where the lessee could renew the license without authorization from the lessor. The bank holding company may arrange for a third party to provide these services or products.

are permissible for bank holding companies under this subpart C.

(5) *Trust company functions.* Performing functions or activities that may be performed by a trust company (including activities of a fiduciary, agency, or custodial nature), in the manner authorized by federal or state law, so long as the company is not a bank for purposes of section 2(c) of the Bank Holding Company Act.

(6) *Financial and investment advisory activities.* Acting as investment or financial advisor to any person, including (without, in any way, limiting the foregoing):

(i) Serving as investment adviser (as defined in section 2(a)(20) of the Investment Company Act of 1940, 15 U.S.C. 80a–2(a)(20)), to an investment company registered under that act, including sponsoring, organizing, and managing a closed-end investment company;

(ii) Furnishing general economic information and advice, general economic statistical forecasting services, and industry studies;

(iii) Providing advice in connection with mergers, acquisitions, divestitures, investments, joint ventures, leveraged buyouts, recapitalizations, capital structurings, financing transactions and similar transactions, and conducting financial feasibility studies;[6]

(iv) Providing information, statistical forecasting, and advice with respect to any transaction in foreign exchange, swaps, and similar transactions, commodities, and any forward contract, option, future, option on a future, and similar instruments;

(v) Providing educational courses, and instructional materials to consumers on individual financial management matters; and

(vi) Providing tax-planning and tax-preparation services to any person.

(7) *Agency transactional services for customer investments*—(i) *Securities brokerage.* Providing securities brokerage services (including securities clearing and/or securities execution services on an exchange), whether alone or in combination with investment advisory services, and incidental activities (including related securities credit activities and custodial services), if the securities brokerage services are restricted to buying and selling securities solely as agent for the account of customers and do not include securities underwriting or dealing.

(ii) *Riskless principal transactions.* Buying and selling in the secondary market all types of securities on the order of customers as a ''riskless principal'' to the extent of engaging in a transaction in which the company, after receiving an order to buy (or sell) a security from a customer, purchases (or sells) the security for its own account to offset a contemporaneous sale to (or purchase from) the customer. This does not include:

(A) Selling bank-ineligible securities[7] at the order of a customer that is the issuer of the securities, or selling bank-ineligible securities in any transaction where the company has a contractual agreement to place the securities as agent of the issuer; or

(B) Acting as a riskless principal in any transaction involving a bank-ineligible security for which the company or any of its affiliates acts as underwriter (during the period of the underwriting or for 30 days thereafter) or dealer.[8]

(iii) *Private placement services.* Acting as agent for the private placement of securities in accordance with the requirements of the Securities Act of 1933 (1933 Act) and the rules of the Securities and Exchange Commission, if the company engaged in the activity does not purchase or repurchase for its own account the securities being placed, or

[6] Feasibility studies do not include assisting management with the planning or marketing for a given project or providing general operational or management advice.

[7] A bank-ineligible security is any security that a State member bank is not permitted to underwrite or deal in under 12 U.S.C. 24 and 335.

[8] A company or its affiliates may not enter quotes for specific bank-ineligible securities in any dealer quotation system in connection with the company's riskless principal transactions; except that the company or its affiliates may enter ''bid'' or ''ask'' quotations, or publish ''offering wanted'' or ''bid wanted'' notices on trading systems other than NASDAQ or an exchange, if the company or its affiliate does not enter price quotations on different sides of the market for a particular security during any two-day period.

hold in inventory unsold portions of issues of these securities.

(iv) *Futures commission merchant.* Acting as a futures commission merchant (FCM) for unaffiliated persons in the execution, clearance, or execution and clearance of any futures contract and option on a futures contract traded on an exchange in the United States or abroad if:

(A) The activity is conducted through a separately incorporated subsidiary of the bank holding company, which may engage in activities other than FCM activities (including, but not limited to, permissible advisory and trading activities); and

(B) The parent bank holding company does not provide a guarantee or otherwise become liable to the exchange or clearing association other than for those trades conducted by the subsidiary for its own account or for the account of any affiliate.

(v) *Other transactional services.* Providing to customers as agent transactional services with respect to swaps and similar transactions, any transaction described in paragraph (b)(8) of this section, any transaction that is permissible for a state member bank, and any other transaction involving a forward contract, option, futures, option on a futures or similar contract (whether traded on an exchange or not) relating to a commodity that is traded on an exchange.

(8) *Investment transactions as principal*—(i) *Underwriting and dealing in government obligations and money market instruments.* Underwriting and dealing in obligations of the United States, general obligations of states and their political subdivisions, and other obligations that state member banks of the Federal Reserve System may be authorized to underwrite and deal in under 12 U.S.C. 24 and 335, including banker's acceptances and certificates of deposit, under the same limitations as would be applicable if the activity were performed by the bank holding company's subsidiary member banks or its subsidiary nonmember banks as if they were member banks.

(ii) *Investing and trading activities.* Engaging as principal in:

(A) Foreign exchange;

(B) Forward contracts, options, futures, options on futures, swaps, and similar contracts, whether traded on exchanges or not, based on any rate, price, financial asset (including gold, silver, platinum, palladium, copper, or any other metal approved by the Board), nonfinancial asset, or group of assets, other than a bank-ineligible security,[9] if:

(*1*) A state member bank is authorized to invest in the asset underlying the contract;

(*2*) The contract requires cash settlement;

(*3*) The contract allows for assignment, termination, or offset prior to delivery or expiration, and the company—

(*i*) Makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract; or

(*ii*) Receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset; or

(*4*) The contract does not allow for assignment, termination, or offset prior to delivery or expiration and is based on an asset for which futures contracts or options on futures contracts have been approved for trading on a U.S. contract market by the Commodity Futures Trading Commission, and the company—

(*i*) Makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract; or

(*ii*) Receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset.

(C) Forward contracts, options,[10] futures, options on futures, swaps, and

[9] A bank-ineligible security is any security that a state member bank is not permitted to underwrite or deal in under 12 U.S.C. 24 and 335.

[10] This reference does not include acting as a dealer in options based on indices of bank-ineligible securities when the options are traded on securities exchanges. These options are securities for purposes of the federal securities laws and bank-ineligible securities for purposes of section 20 of the Glass-Steagall Act, 12 U.S.C. 337. Similarly, this reference does not include acting as a dealer

similar contracts, whether traded on exchanges or not, based on an index of a rate, a price, or the value of any financial asset, nonfinancial asset, or group of assets, if the contract requires cash settlement.

(iii) *Buying and selling bullion, and related activities.* Buying, selling and storing bars, rounds, bullion, and coins of gold, silver, platinum, palladium, copper, and any other metal approved by the Board, for the company's own account and the account of others, and providing incidental services such as arranging for storage, safe custody, assaying, and shipment.

(9) *Management consulting and counseling activities*—(i) *Management consulting.* (A) Providing management consulting advice:[11]

(*1*) On any matter to unaffiliated depository institutions, including commercial banks, savings and loan associations, savings banks, credit unions, industrial banks, Morris Plan banks, cooperative banks, industrial loan companies, trust companies, and branches or agencies of foreign banks;

(*2*) On any financial, economic, accounting, or audit matter to any other company.

(B) A company conducting management consulting activities under this subparagraph and any affiliate of such company may not:

(*1*) Own or control, directly or indirectly, more than 5 percent of the voting securities of the client institution; and

(*2*) Allow a management official, as defined in 12 CFR 212.2(h), of the company or any of its affiliates to serve as a management official of the client institution, except where such interlocking relationship is permitted pursuant to an exemption granted under 12 CFR 212.4(b) or otherwise permitted by the Board.

(C) A company conducting management consulting activities may provide management consulting services to customers not described in paragraph (b)(9)(i)(A)(*1*) of this section or regarding matters not described in paragraph (b)(9)(i)(A)(*2*) of this section, if the total annual revenue derived from those management consulting services does not exceed 30 percent of the company's total annual revenue derived from management consulting activities.

(ii) *Employee benefits consulting services.* Providing consulting services to employee benefit, compensation and insurance plans, including designing plans, assisting in the implementation of plans, providing administrative services to plans, and developing employee communication programs for plans.

(iii) *Career counseling services.* Providing career counseling services to:

(A) A financial organization[12] and individuals currently employed by, or recently displaced from, a financial organization;

(B) Individuals who are seeking employment at a financial organization; and

(C) Individuals who are currently employed in or who seek positions in the finance, accounting, and audit departments of any company.

(10) *Support services*—(i) *Courier services.* Providing courier services for:

(A) Checks, commercial papers, documents, and written instruments (excluding currency or bearer-type negotiable instruments) that are exchanged among banks and financial institutions; and

(B) Audit and accounting media of a banking or financial nature and other business records and documents used in processing such media.[13]

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in any other instrument that is a bank-ineligible security for purposes of section 20. A bank holding company may deal in these instruments in accordance with the Board's orders on dealing in bank-ineligible securities.

[11] In performing this activity, bank holding companies are not authorized to perform tasks or operations or provide services to client institutions either on a daily or continuing basis, except as necessary to instruct the client institution on how to perform such services for itself. See also the Board's interpretation of bank management consulting advice (12 CFR 225.131).

[12] *Financial organization* refers to insured depository institution holding companies and their subsidiaries, other than nonbanking affiliates of diversified savings and loan holding companies that engage in activities not permissible under section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1842(c)(8)).

[13] See also the Board's interpretation on courier activities (12 CFR 225.129), which sets

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(ii) *Printing and selling MICR-encoded items.* Printing and selling checks and related documents, including corporate image checks, cash tickets, voucher checks, deposit slips, savings withdrawal packages, and other forms that require Magnetic Ink Character Recognition (MICR) encoding.

(11) *Insurance agency and underwriting*—(i) *Credit insurance.* Acting as principal, agent, or broker for insurance (including home mortgage redemption insurance) that is:

(A) Directly related to an extension of credit by the bank holding company or any of its subsidiaries; and

(B) Limited to ensuring the repayment of the outstanding balance due on the extension of credit[14] in the event of the death, disability, or involuntary unemployment of the debtor.

(ii) *Finance company subsidiary.* Acting as agent or broker for insurance directly related to an extension of credit by a finance company[15] that is a subsidiary of a bank holding company, if:

(A) The insurance is limited to ensuring repayment of the outstanding balance on such extension of credit in the event of loss or damage to any property used as collateral for the extension of credit; and

(B) The extension of credit is not more than $10,000, or $25,000 if it is to finance the purchase of a residential manufactured home[16] and the credit is secured by the home; and

(C) The applicant commits to notify borrowers in writing that:

(*1*) They are not required to purchase such insurance from the applicant;

(*2*) Such insurance does not insure any interest of the borrower in the collateral; and

(*3*) The applicant will accept more comprehensive property insurance in place of such single-interest insurance.

(iii) *Insurance in small towns.* Engaging in any insurance agency activity in a place where the bank holding company or a subsidiary of the bank holding company has a lending office and that:

(A) Has a population not exceeding 5,000 (as shown in the preceding decennial census); or

(B) Has inadequate insurance agency facilities, as determined by the Board, after notice and opportunity for hearing.

(iv) *Insurance-agency activities conducted on May 1, 1982.* Engaging in any specific insurance-agency activity[17] if the bank holding company, or subsidiary conducting the specific activity, conducted such activity on May 1, 1982, or received Board approval to conduct such activity on or before May 1, 1982.[18] A bank holding company or subsidiary engaging in a specific insurance agency activity under this clause may:

(A) Engage in such specific insurance agency activity only at locations:

(*1*) In the state in which the bank holding company has its principal place of business (as defined in 12 U.S.C. 1842(d));

(*2*) In any state or states immediately adjacent to such state; and

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forth conditions for bank holding company entry into the activity.

[14] *Extension of credit* includes direct loans to borrowers, loans purchased from other lenders, and leases of real or personal property so long as the leases are nonoperating and full-payout leases that meet the requirements of paragraph (b)(3) of this section.

[15] *Finance company* includes all non-deposit-taking financial institutions that engage in a significant degree of consumer lending (excluding lending secured by first mortgages) and all financial institutions specifically defined by individual states as finance companies and that engage in a significant degree of consumer lending.

[16] These limitations increase at the end of each calendar year, beginning with 1982, by the percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers published by the Bureau of Labor Statistics.

[17] Nothing contained in this provision shall preclude a bank holding company subsidiary that is authorized to engage in a specific insurance-agency activity under this clause from continuing to engage in the particular activity after merger with an affiliate, if the merger is for legitimate business purposes and prior notice has been provided to the Board.

[18] For the purposes of this paragraph, activities engaged in on May 1, 1982, include activities carried on subsequently as the result of an application to engage in such activities pending before the Board on May 1, 1982, and approved subsequently by the Board or as the result of the acquisition by such company pursuant to a binding written contract entered into on or before May 1, 1982, of another company engaged in such activities at the time of the acquisition.

(*3*) In any state in which the specific insurance-agency activity was conducted (or was approved to be conducted) by such bank holding company or subsidiary thereof or by any other subsidiary of such bank holding company on May 1, 1982; and

(B) Provide other insurance coverages that may become available after May 1, 1982, so long as those coverages insure against the types of risks as (or are otherwise functionally equivalent to) coverages sold or approved to be sold on May 1, 1982, by the bank holding company or subsidiary.

(v) *Supervision of retail insurance agents.* Supervising on behalf of insurance underwriters the activities of retail insurance agents who sell:

(A) Fidelity insurance and property and casualty insurance on the real and personal property used in the operations of the bank holding company or its subsidiaries; and

(B) Group insurance that protects the employees of the bank holding company or its subsidiaries.

(vi) *Small bank holding companies.* Engaging in any insurance-agency activity if the bank holding company has total consolidated assets of $50 million or less. A bank holding company performing insurance-agency activities under this paragraph may not engage in the sale of life insurance or annuities except as provided in paragraphs (b)(11) (i) and (iii) of this section, and it may not continue to engage in insurance-agency activities pursuant to this provision more than 90 days after the end of the quarterly reporting period in which total assets of the holding company and its subsidiaries exceed $50 million.

(vii) *Insurance-agency activities conducted before 1971.* Engaging in any insurance-agency activity performed at any location in the United States directly or indirectly by a bank holding company that was engaged in insurance-agency activities prior to January 1, 1971, as a consequence of approval by the Board prior to January 1, 1971.

(12) *Community development activities*—(i) *Financing and investment activities.* Making equity and debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas by providing housing, services, or jobs for residents.

(ii) *Advisory activities.* Providing advisory and related services for programs designed primarily to promote community welfare.

(13) *Money orders, savings bonds, and traveler's checks.* The issuance and sale at retail of money orders and similar consumer-type payment instruments; the sale of U.S. savings bonds; and the issuance and sale of traveler's checks.

(14) *Data processing.* (i) Providing data processing, data storage and data transmission services, facilities (including data processing, data storage and data transmission hardware, software, documentation, or operating personnel), databases, advice, and access to such services, facilities, or databases by any technological means, if:

(A) The data to be processed, stored or furnished are financial, banking or economic; and

(B) The hardware provided in connection therewith is offered only in conjunction with software designed and marketed for the processing, storage and transmission of financial, banking, or economic data, and where the general purpose hardware does not constitute more than 30 percent of the cost of any packaged offering.

(ii) A company conducting data processing, data storage, and data transmission activities may conduct data processing, data storage, and data transmission activities not described in paragraph (b)(14)(i) of this section if the total annual revenue derived from those activities does not exceed 49 percent of the company's total annual revenues derived from data processing, data storage and data transmission activities.

[Reg. Y, 62 FR 9329, Feb. 28, 1997, as amended at 68 FR 39810, July 3, 2003; 68 FR 41901, July 16, 2003; 68 FR 68499, Dec. 9, 2003]

Subpart D—Control and Divestiture Proceedings

§ 225.31 Control proceedings.

(a) *Preliminary determination of control.* (1) The Board may issue a preliminary determination of control under the procedures set forth in this section in any case in which:

(i) Any of the presumptions of control set forth in paragraph (d) of this section is present; or

(ii) It otherwise appears that a company has the power to exercise a controlling influence over the management or policies of a bank or other company.

(2) If the Board makes a preliminary determination of control under this section, the Board shall send notice to the controlling company containing a statement of the facts upon which the preliminary determination is based.

(b) *Response to preliminary determination of control.* Within 30 calendar days of issuance by the Board of a preliminary determination of control or such longer period permitted by the Board, the company against whom the determination has been made shall:

(1) Submit for the Board's approval a specific plan for the prompt termination of the control relationship;

(2) File an application under subpart B or C of this regulation to retain the control relationship; or

(3) Contest the preliminary determination by filing a response, setting forth the facts and circumstances in support of its position that no control exists, and, if desired, requesting a hearing or other proceeding.

(c) *Hearing and final determination.* (1) The Board shall order a formal hearing or other appropriate proceeding upon the request of a company that contests a preliminary determination that the company has the power to exercise a controlling influence over the management or policies of a bank or other company, if the Board finds that material facts are in dispute. The Board may also in its discretion order a formal hearing or other proceeding with respect to a preliminary determination that the company controls voting securities of the bank or other company under the presumptions in paragraph (d)(1) of this section.

(2) At a hearing or other proceeding, any applicable presumptions established by paragraph (d) of this section shall be considered in accordance with the Federal Rules of Evidence and the Board's Rules of Practice for Formal Hearings (12 CFR part 263).

(3) After considering the submissions of the company and other evidence, including the record of any hearing or other proceeding, the Board shall issue a final order determining whether the company controls voting securities, or has the power to exercise a controlling influence over the management or policies, of the bank or other company. If a control relationship is found, the Board may direct the company to terminate the control relationship or to file an application for the Board's approval to retain the control relationship under subpart B or C of this regulation.

(d) *Rebuttable presumptions of control.* The following rebuttable presumptions shall be used in any proceeding under this section:

(1) *Control of voting securities*—(i) *Securities convertible into voting securities.* A company that owns, controls, or holds securities that are immediately convertible, at the option of the holder or owner, into voting securities of a bank or other company, controls the voting securities.

(ii) *Option or restriction on voting securities.* A company that enters into an agreement or understanding under which the rights of a holder of voting securities of a bank or other company are restricted in any manner controls the securities. This presumption does not apply where the agreement or understanding:

(A) Is a mutual agreement among shareholders granting to each other a right of first refusal with respect to their shares;

(B) Is incident to a *bona fide* loan transaction; or

(C) Relates to restrictions on transferability and continues only for the time necessary to obtain approval from the appropriate Federal supervisory authority with respect to acquisition by the company of the securities.

(2) *Control over company*—(i) *Management agreement.* A company that enters into any agreement or understanding with a bank or other company (other than an investment advisory agreement), such as a management contract, under which the first company or any of its subsidiaries directs or exercises significant influence over the general management or overall operations of the bank or other company controls the bank or other company.

(ii) *Shares controlled by company and associated individuals.* A company that, together with its management officials or controlling shareholders (including members of the immediate families of either), owns, controls, or holds with power to vote 25 percent or more of the outstanding shares of any class of voting securities of a bank or other company controls the bank or other company, if the first company owns, controls, or holds with power to vote more than 5 percent of the outstanding shares of any class of voting securities of the bank or other company.

(iii) *Common management officials.* A company that has one or more management officials in common with a bank or other company controls the bank or other company, if the first company owns, controls or holds with power to vote more than 5 percent of the outstanding shares of any class of voting securities of the bank or other company, and no other person controls as much as 5 percent of the outstanding shares of any class of voting securities of the bank or other company.

(iv) *Shares held as fiduciary.* The presumptions in paragraphs (d)(2) (ii) and (iii) of this section do not apply if the securities are held by the company in a fiduciary capacity without sole discretionary authority to exercise the voting rights.

(e) *Presumption of non-control*—(1) In any proceeding under this section, there is a presumption that any company that directly or indirectly owns, controls, or has power to vote less than 5 percent of the outstanding shares of any class of voting securities of a bank or other company does not have control over that bank or other company.

(2) In any proceeding under this section, or judicial proceeding under the BHC Act, other than a proceeding in which the Board has made a preliminary determination that a company has the power to exercise a controlling influence over the management or policies of the bank or other company, a company may not be held to have had control over the bank or other company at any given time, unless that company, at the time in question, directly or indirectly owned, controlled, or had power to vote 5 percent or more of the outstanding shares of any class of voting securities of the bank or other company, or had already been found to have control on the basis of the existence of a controlling influence relationship.

[Reg. Y, 49 FR 818, Jan. 5, 1984, as amended at 58 FR 474, Jan. 6, 1993; Reg. Y, 62 FR 9338, Feb. 28, 1997]

Subpart E—Change in Bank Control

SOURCE: Reg. Y, 62 FR 9338, Feb. 28, 1997, unless otherwise noted.

§ 225.41 Transactions requiring prior notice.

(a) *Prior notice requirement.* Any person acting directly or indirectly, or through or in concert with one or more persons, shall give the Board 60 days' written notice, as specified in § 225.43 of this subpart, before acquiring control of a state member bank or bank holding company, unless the acquisition is exempt under § 225.42.

(b) *Definitions.* For purposes of this subpart:

(1) *Acquisition* includes a purchase, assignment, transfer, or pledge of voting securities, or an increase in percentage ownership of a state member bank or a bank holding company resulting from a redemption of voting securities.

(2) *Acting in concert* includes knowing participation in a joint activity or parallel action towards a common goal of acquiring control of a state member bank or bank holding company whether or not pursuant to an express agreement.

(3) *Immediate family* includes a person's father, mother, stepfather, stepmother, brother, sister, stepbrother, stepsister, son, daughter, stepson, stepdaughter, grandparent, grandson, granddaughter, father-in-law, mother-in-law, brother-in-law, sister-in-law, son-in-law, daughter-in-law, the spouse of any of the foregoing, and the person's spouse.

(c) *Acquisitions requiring prior notice*—(1) *Acquisition of control.* The acquisition of voting securities of a state member bank or bank holding company constitutes the acquisition of control under the Bank Control Act, requiring

prior notice to the Board, if, immediately after the transaction, the acquiring person (or persons acting in concert) will own, control, or hold with power to vote 25 percent or more of any class of voting securities of the institution.

(2) *Rebuttable presumption of control.* The Board presumes that an acquisition of voting securities of a state member bank or bank holding company constitutes the acquisition of control under the Bank Control Act, requiring prior notice to the Board, if, immediately after the transaction, the acquiring person (or persons acting in concert) will own, control, or hold with power to vote 10 percent or more of any class of voting securities of the institution, and if:

(i) The institution has registered securities under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l); or

(ii) No other person will own, control, or hold the power to vote a greater percentage of that class of voting securities immediately after the transaction.[1]

(d) *Rebuttable presumption of concerted action.* The following persons shall be presumed to be acting in concert for purposes of this subpart:

(1) A company and any controlling shareholder, partner, trustee, or management official of the company, if both the company and the person own voting securities of the state member bank or bank holding company;

(2) An individual and the individual's immediate family;

(3) Companies under common control;

(4) Persons that are parties to any agreement, contract, understanding, relationship, or other arrangement, whether written or otherwise, regarding the acquisition, voting, or transfer of control of voting securities of a state member bank or bank holding company, other than through a revocable proxy as described in §225.42(a)(5) of this subpart;

(5) Persons that have made, or propose to make, a joint filing under sections 13 or 14 of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78n), and the rules promulgated thereunder by the Securities and Exchange Commission; and

(6) A person and any trust for which the person serves as trustee.

(e) *Acquisitions of loans in default.* The Board presumes an acquisition of a loan in default that is secured by voting securities of a state member bank or bank holding company to be an acquisition of the underlying securities for purposes of this section.

(f) *Other transactions.* Transactions other than those set forth in paragraph (c) of this section resulting in a person's control of less than 25 percent of a class of voting securities of a state member bank or bank holding company are not deemed by the Board to constitute control for purposes of the Bank Control Act.

(g) *Rebuttal of presumptions.* Prior notice to the Board is not required for any acquisition of voting securities under the presumption of control set forth in this section, if the Board finds that the acquisition will not result in control. The Board shall afford any person seeking to rebut a presumption in this section an opportunity to present views in writing or, if appropriate, orally before its designated representatives at an informal conference.

§225.42 Transactions not requiring prior notice.

(a) *Exempt transactions.* The following transactions do not require notice to the Board under this subpart:

(1) *Existing control relationships.* The acquisition of additional voting securities of a state member bank or bank holding company by a person who:

(i) Continuously since March 9, 1979 (or since the institution commenced business, if later), held power to vote 25 percent or more of any class of voting securities of the institution; or

(ii) Is presumed, under §225.41(c)(2) of this subpart, to have controlled the institution continuously since March 9, 1979, if the aggregate amount of voting securities held does not exceed 25 percent or more of any class of voting securities of the institution or, in other

[1] If two or more persons, not acting in concert, each propose to acquire simultaneously equal percentages of 10 percent or more of a class of voting securities of the state member bank or bank holding company, each person must file prior notice to the Board.

cases, where the Board determines that the person has controlled the bank continuously since March 9, 1979;

(2) *Increase of previously authorized acquisitions.* Unless the Board or the Reserve Bank otherwise provides in writing, the acquisition of additional shares of a class of voting securities of a state member bank or bank holding company by any person (or persons acting in concert) who has lawfully acquired and maintained control of the institution (for purposes of § 225.41(c) of this subpart), after complying with the procedures and receiving approval to acquire voting securities of the institution under this subpart, or in connection with an application approved under section 3 of the BHC Act (12 U.S.C. 1842; § 225.11 of subpart B of this part) or section 18(c) of the Federal Deposit Insurance Act (Bank Merger Act, 12 U.S.C. 1828(c));

(3) *Acquisitions subject to approval under BHC Act or Bank Merger Act.* Any acquisition of voting securities subject to approval under section 3 of the BHC Act (12 U.S.C. 1842; § 225.11 of subpart B of this part), or section 18(c) of the Federal Deposit Insurance Act (Bank Merger Act, 12 U.S.C. 1828(c));

(4) *Transactions exempt under BHC Act.* Any transaction described in sections 2(a)(5), 3(a)(A), or 3(a)(B) of the BHC Act (12 U.S.C. 1841(a)(5), 1842(a)(A), and 1842(a)(B)), by a person described in those provisions;

(5) *Proxy solicitation.* The acquisition of the power to vote securities of a state member bank or bank holding company through receipt of a revocable proxy in connection with a proxy solicitation for the purposes of conducting business at a regular or special meeting of the institution, if the proxy terminates within a reasonable period after the meeting;

(6) *Stock dividends.* The receipt of voting securities of a state member bank or bank holding company through a stock dividend or stock split if the proportional interest of the recipient in the institution remains substantially the same; and

(7) *Acquisition of foreign banking organization.* The acquisition of voting securities of a qualifying foreign banking organization. (This exemption does not extend to the reports and information required under paragraphs 9, 10, and 12 of the Bank Control Act (12 U.S.C. 1817(j) (9), (10), and (12)) and § 225.44 of this subpart.)

(b) *Prior notice exemption.* (1) The following acquisitions of voting securities of a state member bank or bank holding company, which would otherwise require prior notice under this subpart, are not subject to the prior notice requirements if the acquiring person notifies the appropriate Reserve Bank within 90 calendar days after the acquisition and provides any relevant information requested by the Reserve Bank:

(i) Acquisition of voting securities through inheritance;

(ii) Acquisition of voting securities as a *bona fide* gift; and

(iii) Acquisition of voting securities in satisfaction of a debt previously contracted (DPC) in good faith.

(2) The following acquisitions of voting securities of a state member bank or bank holding company, which would otherwise require prior notice under this subpart, are not subject to the prior notice requirements if the acquiring person does not reasonably have advance knowledge of the transaction, and provides the written notice required under section 225.43 to the appropriate Reserve Bank within 90 calendar days after the transaction occurs:

(i) Acquisition of voting securities resulting from a redemption of voting securities by the issuing bank or bank holding company; and

(ii) Acquisition of voting securities as a result of actions (including the sale of securities) by any third party that is not within the control of the acquiror.

(3) Nothing in paragraphs (b)(1) or (b)(2) of this section limits the authority of the Board to disapprove a notice pursuant to § 225.43(h) of this subpart.

§ 225.43 Procedures for filing, processing, publishing, and acting on notices.

(a) *Filing notice.* (1) A notice required under this subpart shall be filed with the appropriate Reserve Bank and shall contain all the information required by paragraph 6 of the Bank Control Act (12 U.S.C. 1817(j)(6)), or prescribed in the designated Board form.

(2) The Board may waive any of the informational requirements of the notice if the Board determines that it is in the public interest.

(3) A notificant shall notify the appropriate Reserve Bank or the Board immediately of any material changes in a notice submitted to the Reserve Bank, including changes in financial or other conditions.

(4) When the acquiring person is an individual, or group of individuals acting in concert, the requirement to provide personal financial data may be satisfied by a current statement of assets and liabilities and an income summary, as required in the designated Board form, together with a statement of any material changes since the date of the statement or summary. The Reserve Bank or the Board, nevertheless, may request additional information, if appropriate.

(b) *Acceptance of notice.* The 60-day notice period specified in §225.41 of this subpart begins on the date of receipt of a complete notice. The Reserve Bank shall notify the person or persons submitting a notice under this subpart in writing of the date the notice is or was complete and thereby accepted for processing. The Reserve Bank or the Board may request additional relevant information at any time after the date of acceptance.

(c) *Publication*—(1) *Newspaper Announcement.* Any person(s) filing a notice under this subpart shall publish, in a form prescribed by the Board, an announcement soliciting public comment on the proposed acquisition. The announcement shall be published in a newspaper of general circulation in the community in which the head office of the state member bank to be acquired is located or, in the case of a proposed acquisition of a bank holding company, in the community in which its head office is located and in the community in which the head office of each of its subsidiary banks is located. The announcement shall be published no earlier than 15 calendar days before the filing of the notice with the appropriate Reserve Bank and no later than 10 calendar days after the filing date; and the publisher's affidavit of a publication shall be provided to the appropriate Reserve Bank.

(2) *Contents of newspaper announcement.* The newspaper announcement shall state:

(i) The name of each person identified in the notice as a proposed acquiror of the bank or bank holding company;

(ii) The name of the bank or bank holding company to be acquired, including the name of each of the bank holding company's subsidiary banks; and

(iii) A statement that interested persons may submit comments on the notice to the Board or the appropriate Reserve Bank for a period of 20 days, or such shorter period as may be provided, pursuant to paragraph (c)(5) of this section.

(3) FEDERAL REGISTER *announcement.* The Board shall, upon filing of a notice under this subpart, publish announcement in the FEDERAL REGISTER of receipt of the notice. The FEDERAL REGISTER announcement shall contain the information required under paragraphs (c)(2)(i) and (c)(2)(ii) of this section and a statement that interested persons may submit comments on the proposed acquisition for a period of 15 calendar days, or such shorter period as may be provided, pursuant to paragraph (c)(5) of this section. The Board may waive publication in the FEDERAL REGISTER, if the Board determines that such action is appropriate.

(4) *Delay of publication.* The Board may permit delay in the publication required under paragraphs (c)(1) and (c)(3) of this section if the Board determines, for good cause shown, that it is in the public interest to grant such delay. Requests for delay of publication may be submitted to the appropriate Reserve Bank.

(5) *Shortening or waiving notice.* The Board may shorten or waive the public comment or newspaper publication requirements of this paragraph, or act on a notice before the expiration of a public comment period, if it determines in writing that an emergency exists, or that disclosure of the notice, solicitation of public comment, or delay until expiration of the public comment period would seriously threaten the safety or soundness of the bank or bank holding company to be acquired.

(6) *Consideration of public comments.* In acting upon a notice filed under this subpart, the Board shall consider all public comments received in writing within the period specified in the newspaper or FEDERAL REGISTER announcement, whichever is later. At the Board's option, comments received after this period may, but need not, be considered.

(7) *Standing.* No person (other than the acquiring person) who submits comments or information on a notice filed under this subpart shall thereby become a party to the proceeding or acquire any standing or right to participate in the Board's consideration of the notice or to appeal or otherwise contest the notice or the Board's action regarding the notice.

(d) *Time period for Board action*—(1) *Consummation of acquisition*—(i) The notificant(s) may consummate the proposed acquisition 60 days after submission to the Reserve Bank of a complete notice under paragraph (a) of this section, unless within that period the Board disapproves the proposed acquisition or extends the 60-day period, as provided under paragraph (d)(2) of this section.

(ii) The notificant(s) may consummate the proposed transaction before the expiration of the 60-day period if the Board notifies the notificant(s) in writing of the Board's intention not to disapprove the acquisition.

(2) *Extensions of time period.* (i) The Board may extend the 60-day period in paragraph (d)(1) of this section for an additional 30 days by notifying the acquiring person(s).

(ii) The Board may further extend the period during which it may disapprove a notice for two additional periods of not more than 45 days each, if the Board determines that:

(A) Any acquiring person has not furnished all the information required under paragraph (a) of this section;

(B) Any material information submitted is substantially inaccurate;

(C) The Board is unable to complete the investigation of an acquiring person because of inadequate cooperation or delay by that person; or

(D) Additional time is needed to investigate and determine that no acquiring person has a record of failing to comply with the requirements of the Bank Secrecy Act, subchapter II of Chapter 53 of Title 31, United States Code.

(iii) If the Board extends the time period under this paragraph, it shall notify the acquiring person(s) of the reasons therefor and shall include a statement of the information, if any, deemed incomplete or inaccurate.

(e) *Advice to bank supervisory agencies.* (1) Upon accepting a notice relating to acquisition of securities of a state member bank, the Reserve Bank shall send a copy of the notice to the appropriate state bank supervisor, which shall have 30 calendar days from the date the notice is sent in which to submit its views and recommendations to the Board. The Reserve Bank also shall send a copy of any notice to the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision.

(2) If the Board finds that it must act immediately in order to prevent the probable failure of the bank or bank holding company involved, the Board may dispense with or modify the requirements for notice to the state supervisor.

(f) *Investigation and report.* (1) After receiving a notice under this subpart, the Board or the appropriate Reserve Bank shall conduct an investigation of the competence, experience, integrity, and financial ability of each person by and for whom an acquisition is to be made. The Board shall also make an independent determination of the accuracy and completeness of any information required to be contained in a notice under paragraph (a) of this section. In investigating any notice accepted under this subpart, the Board or Reserve Bank may solicit information or views from any person, including any bank or bank holding company involved in the notice, and any appropriate state, federal, or foreign governmental authority.

(2) The Board or the appropriate Reserve Bank shall prepare a written report of its investigation, which shall contain, at a minimum, a summary of the results of the investigation.

(g) *Factors considered in acting on notices.* In reviewing a notice filed under this subpart, the Board shall consider

the information in the record, the views and recommendations of the appropriate bank supervisor, and any other relevant information obtained during any investigation of the notice.

(h) *Disapproval and hearing*—(1) *Disapproval of notice.* The Board may disapprove an acquisition if it finds adverse effects with respect to any of the factors set forth in paragraph 7 of the Bank Control Act (12 U.S.C. 1817(j)(7)) (*i.e.,* competitive, financial, managerial, banking, or incompleteness of information).

(2) *Disapproval notification.* Within three days after its decision to issue a notice of intent to disapprove any proposed acquisition, the Board shall notify the acquiring person in writing of the reasons for the action.

(3) *Hearing.* Within 10 calendar days of receipt of the notice of the Board's intent to disapprove, the acquiring person may submit a written request for a hearing. Any hearing conducted under this paragraph shall be in accordance with the Rules of Practice for Formal Hearings (12 CFR part 263). At the conclusion of the hearing, the Board shall, by order, approve or disapprove the proposed acquisition on the basis of the record of the hearing. If the acquiring person does not request a hearing, the notice of intent to disapprove becomes final and unappealable.

§ 225.44 Reporting of stock loans.

(a) *Requirements.* (1) Any foreign bank or affiliate of a foreign bank that has credit outstanding to any person or group of persons, in the aggregate, which is secured, directly or indirectly, by 25 percent or more of any class of voting securities of a state member bank, shall file a consolidated report with the appropriate Reserve Bank for the state member bank.

(2) The foreign bank or its affiliate also shall file a copy of the report with its appropriate Federal banking agency.

(3) Any shares of the state member bank held by the foreign bank or any affiliate of the foreign bank as principal must be included in the calculation of the number of shares in which the foreign bank or its affiliate has a security interest for purposes of paragraph (a) of this section.

(b) *Definitions.* For purposes of paragraph (a) of this section:

(1) *Foreign bank* shall have the same meaning as in section 1(b) of the International Banking Act of 1978 (12 U.S.C. 3101).

(2) *Credit outstanding* includes any loan or extension of credit; the issuance of a guarantee, acceptance, or letter of credit, including an endorsement or standby letter of credit; and any other type of transaction that extends credit or financing to the person or group of persons.

(3) *Group of persons* includes any number of persons that the foreign bank or any affiliate of a foreign bank has reason to believe:

(i) Are acting together, in concert, or with one another to acquire or control shares of the same insured depository institution, including an acquisition of shares of the same depository institution at approximately the same time under substantially the same terms; or

(ii) Have made, or propose to make, a joint filing under section 13 or 14 of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78n), and the rules promulgated thereunder by the Securities and Exchange Commission regarding ownership of the shares of the same insured depository institution.

(c) *Exceptions.* Compliance with paragraph (a) of this section is not required if:

(1) The person or group of persons referred to in that paragraph has disclosed the amount borrowed and the security interest therein to the Board or appropriate Reserve Bank in connection with a notice filed under § 225.41 of this subpart, or another application filed with the Board or Reserve Bank as a substitute for a notice under § 225.41 of this subpart, including an application filed under section 3 of the BHC Act (12 U.S.C. 1842) or section 18(c) of the Federal Deposit Insurance Act (Bank Merger Act, 12 U.S.C. 1828(c)), or an application for membership in the Federal Reserve System; or

(2) The transaction involves a person or group of persons that has been the owner or owners of record of the stock for a period of one year or more; or, if the transaction involves stock issued by a newly chartered bank, before the bank is opened for business.

(d) *Report requirements.* (1) The consolidated report shall indicate the number and percentage of shares securing each applicable extension of credit, the identity of the borrower, and the number of shares held as principal by the foreign bank and any affiliate thereof.

(2) A foreign bank, or any affiliate of a foreign bank, shall file the consolidated report in writing within 30 days of the date on which the foreign bank or affiliate first believes that the security for any outstanding credit consists of 25 percent or more of any class of voting securities of a state member bank.

(e) *Other reporting requirements.* A foreign bank, or any affiliate thereof, that is supervised by the System and is required to report credit outstanding that is secured by the shares of an insured depository institution to another Federal banking agency also shall file a copy of the report with the appropriate Reserve Bank.

Subpart F—Limitations on Nonbank Banks

§ 225.52 Limitation on overdrafts.

(a) *Definitions.* For purposes of this section—

(1) *Account* means a reserve account, clearing account, or deposit account as defined in the Board's Regulation D (12 CFR 204.2(a)(1)(i)), that is maintained at a Federal Reserve Bank or nonbank bank.

(2) *Cash item* means (i) a check other than a check classified as a noncash item; or (ii) any other item payable on demand and collectible at par that the Federal Reserve Bank of the district in which the item is payable is willing to accept as a cash item.

(3) *Discount window loan* means any credit extended by a Federal Reserve Bank to a nonbank bank or industrial bank pursuant to the provisions of the Board's Regulation A (12 CFR part 201).

(4) *Industrial bank* means an institution as defined in section 2(c)(2)(H) of the BHC Act (12 U.S.C. 1841(c)(2)(H)).

(5) *Noncash item* means an item handled by a Reserve Bank as a noncash item under the Reserve Bank's ''Collection of Noncash Items Operating Circular'' (*e.g.*, a maturing bankers' acceptance or a maturing security, or a demand item, such as a check, with special instructions or an item that has not been preprinted or post-encoded).

(6) *Other nonelectronic transactions* include all other transactions not included as funds transfers, book-entry securities transfers, cash items, noncash items, automated clearing house transactions, net settlement entries, and discount window loans (*e.g.*, original issue of securities or redemption of securities).

(7) An *overdraft* in an account occurs whenever the Federal Reserve Bank, nonbank bank, or industrial bank holding an account posts a transaction to the account of the nonbank bank, industrial bank, or affiliate that exceeds the aggregate balance of the accounts of the nonbank bank, industrial bank, or affiliate, as determined by the posting rules set forth in paragraphs (d) and (e) of this section and continues until the aggregate balance of the account is zero or greater.

(8) *Transfer item* means an item as defined in subpart B of Regulation J (12 CFR 210.25 *et seq*).

(b) *Restriction on overdrafts*—(1) *Affiliates.* Neither a nonbank bank nor an industrial bank shall permit any affiliate to incur any overdraft in its account with the nonbank bank or industrial bank.

(2) *Nonbank banks or industrial banks.* (i) No nonbank bank or industrial bank shall incur any overdraft in its account at a Federal Reserve Bank on behalf of an affiliate.

(ii) An overdraft by a nonbank bank or industrial bank in its account at a Federal Reserve Bank shall be deemed to be on behalf of an affiliate whenever:

(A) A nonbank bank or industrial bank holds an account for an affiliate from which third-party payments can be made; and

(B) When the posting of an affiliate's transaction to the nonbank bank's or industrial bank's account at a Reserve Bank creates an overdraft in its account at a Federal Reserve Bank or increases the amount of an existing overdraft in its account at a Federal Reserve Bank.

(c) *Permissible overdrafts.* The following are permissible overdrafts not subject to paragraph (b) of this section:

(1) *Inadvertent error.* An overdraft in its account by a nonbank bank or its affiliate, or an industrial bank or its affiliate, that results from an inadvertent computer error or inadvertent accounting error, that was not reasonably forseeable or could not have been prevented through the maintenance of procedures reasonably adopted by the nonbank bank or affiliate to avoid such overdraft; and

(2) *Fully secured primary dealer affiliate overdrafts.* (i) An overdraft incurred by an affiliate of a nonbank bank, which affiliate is recognized as a primary dealer by the Federal Reserve Bank of New York, in the affiliate's account at the nonbank bank, or an overdraft incurred by a nonbank bank on behalf of its primary dealer affiliate in the nonbank bank's account at a Federal Reserve Bank; *provided:* the overdraft is fully secured by bonds, notes, or other obligations which are direct obligations of the United States or on which the principal and interest are fully guaranteed by the United States or by securities and obligations eligible for settlement on the Federal Reserve book-entry system.

(ii) An overdraft by a nonbank bank in its account at a Federal Reserve Bank that is on behalf of a primary dealer affiliate is fully secured when that portion of its overdraft at the Federal Reserve Bank that corresponds to the transaction posted for an affiliate that caused or increased the nonbank bank's overdraft is fully secured in accordance with paragraph (c)(2)(iii) of this section.

(iii) An overdraft is fully secured under paragraph (c)(2)(i) when the nonbank bank can demonstrate that the overdraft is secured, at all times, by a perfected security interest in specific, identified obligations described in paragraph (c)(2)(i) with a market value that, in the judgment of the Reserve Bank holding the nonbank bank's account, is sufficiently in excess of the amount of the overdraft to provide a margin of protection in a volatile market or in the event the securities need to be liquidated quickly.

(d) *Posting by Federal Reserve Banks.* For purposes of determining the balance of an account under this section, payments and transfers by nonbank banks and industrial banks processed by the Federal Reserve Banks shall be considered posted to their accounts at Federal Reserve Banks as follows:

(1) *Funds transfers.* Transfer items shall be posted:

(i) To the transferor's account at the time the transfer is actually made by the transferor's Federal Reserve Bank; and

(ii) To the transferee's account at the time the transferee's Reserve Bank sends the transfer item or sends or telephones the advice of credit for the item to the transferee, whichever occurs first.

(2) *Book-entry securities transfers against payment.* A book-entry securities transfer against payment shall be posted: (i) to the transferor's account at the time the entry is made by the transferor's Reserve Bank; and (ii) to the transferee's account at the time the entry is made by the transferee's Reserve Bank.

(3) *Discount window loans.* Credit for a discount window loan shall be posted to the account of a nonbank bank or industrial bank at the close of business on the day that it is made or such earlier time as may be specifically agreed to by the Federal Reserve Bank and the nonbank bank under the terms of the loan. Debit for repayment of a discount window loan shall be posted to the account of the nonbank bank or industrial bank as of the close of business on the day of maturity of the loan or such earlier time as may be agreed to by the Federal Reserve Bank and the nonbank bank or required by the Federal Reserve Bank under the terms of the loan.

(4) *Other transactions.* Total aggregate credits for automated clearing house transfers, cash items, noncash items, net settlement entries, and other nonelectronic transactions shall be posted to the account of a nonbank bank or industrial bank as of the opening of business on settlement day. Total aggregate debits for these transactions and entries shall be posted to the account of a nonbank bank or industrial

bank as of the close of business on settlement day.

(e) *Posting by nonbank banks and industrial banks.* For purposes of determining the balance of an affiliate's account under this section, payments and transfers through an affiliate's account at a nonbank bank or industrial bank shall be posted as follows:

(1) *Funds transfers.* (i) Fedwire transfer items shall be posted:

(A) To the transferor affiliate's account no later than the time the transfer is actually made by the transferor's Federal Reserve Bank; and

(B) To the transferee affiliate's account no earlier than the time the transferee's Reserve Bank sends the transfer item, or sends or telephones the advice of credit for the item to the transferee, whichever occurs first.

(ii) For funds transfers not sent or received through Federal Reserve Banks, debits shall be posted to the transferor affiliate's account not later than the time the nonbank bank or industrial bank becomes obligated on the transfer. Credits shall not be posted to the transferee affiliate's account before the nonbank bank or industrial bank has received actually and finally collected funds for the transfer.

(2) *Book-entry securities transfers against payment.* (i) A book-entry securities transfer against payment shall be posted:

(A) To the transferor affiliate's account not earlier than the time the entry is made by the transferor's Reserve Bank; and

(B) To the transferee affiliate's account not later than the time the entry is made by the transferee's Reserve Bank.

(ii) For book-entry securities transfers against payment that are not sent or received through Federal Reserve Banks, entries shall be posted:

(A) To the buyer-affiliate's account not later than the time the nonbank bank or industrial bank becomes obligated on the transfer; and

(B) To the seller-affiliate's account not before the nonbank bank or industrial bank has received actually and finally collected funds for the transfer.

(3) *Other transactions*—(i) *Credits.* Except as otherwise provided in this paragraph, credits for cash items, noncash items, ACH transfers, net settlement entries, and all other nonelectronic transactions shall be posted to an affiliate's account on the day of the transaction (*i.e.,* settlement day for ACH transactions or the day of credit for check transactions), but no earlier than the Federal Reserve Bank's opening of business on that day. Credit for cash items that are required by federal or state statute or regulation to be made available to the depositor for withdrawal prior to the posting time set forth in the preceding paragraph shall be posted as of the required availability time.

(ii) *Debits.* Debits for cash items, noncash items, ACH transfers, net settlement entries, and all other nonelectronic transactions shall be posted to an affiliate's account on the day of the transaction (*e.g.,* settlement day for ACH transactions or the day of presentment for check transactions), but no later than the Federal Reserve Bank's close of business on that day. If a check drawn on an affiliate's account or an ACH debit transfer received by an affiliate is returned timely by the nonbank bank or industrial bank in accordance with applicable law and agreements, no entry need to be posted to the affiliate's account for such item.

[Reg. Y, 53 FR 37744, Sept. 28, 1988]

Subpart G—Appraisal Standards for Federally Related Transactions

SOURCE: Reg. Y, 55 FR 27771, July 5, 1990, unless otherwise noted.

§ 225.61 Authority, purpose, and scope.

(a) *Authority.* This subpart is issued by the Board of Governors of the Federal Reserve System (the *Board*) under title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (*FIRREA*) (Pub. L. No. 101–73, 103 Stat. 183 (1989)), 12 U.S.C. 3310, 3331–3351, and section 5(b) of the Bank Holding Company Act, 12 U.S.C. 1844(b).

(b) *Purpose and scope.* (1) Title XI provides protection for federal financial and public policy interests in real estate related transactions by requiring real estate appraisals used in connection with federally related transactions

to be performed in writing, in accordance with uniform standards, by appraisers whose competency has been demonstrated and whose professional conduct will be subject to effective supervision. This subpart implements the requirements of title XI, and applies to all federally related transactions entered into by the Board or by institutions regulated by the Board (*regulated institutions*).

(2) This subpart:

(i) Identifies which real estate-related financial transactions require the services of an appraiser;

(ii) Prescribes which categories of federally related transactions shall be appraised by a State certified appraiser and which by a State licensed appraiser; and

(iii) Prescribes minimum standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of the Board.

§ 225.62 Definitions.

(a) *Appraisal* means a written statement independently and impartially prepared by a qualified appraiser setting forth an opinion as to the market value of an adequately described property as of a specific date(s), supported by the presentation and analysis of relevant market information.

(b) *Appraisal Foundation* means the Appraisal Foundation established on November 30, 1987, as a not-for-profit corporation under the laws of Illinois.

(c) *Appraisal Subcommittee* means the Appraisal Subcommittee of the Federal Financial Institutions Examination Council.

(d) *Business loan* means a loan or extension of credit to any corporation, general or limited partnership, business trust, joint venture, pool, syndicate, sole proprietorship, or other business entity.

(e) *Complex 1-to-4 family residential property appraisal* means one in which the property to be appraised, the form of ownership, or market conditions are atypical.

(f) *Federally related transaction* means any real estate-related financial transaction entered into on or after August 9, 1990, that:

(1) The Board or any regulated institution engages in or contracts for; and

(2) Requires the services of an appraiser.

(g) *Market value* means the most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

(1) Buyer and seller are typically motivated;

(2) Both parties are well informed or well advised, and acting in what they consider their own best interests;

(3) A reasonable time is allowed for exposure in the open market;

(4) Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and

(5) The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

(h) *Real estate* or *real property* means an identified parcel or tract of land, with improvements, and includes easements, rights of way, undivided or future interests, or similar rights in a tract of land, but does not include mineral rights, timber rights, growing crops, water rights, or similar interests severable from the land when the transaction does not involve the associated parcel or tract of land.

(i) *Real estate-related financial transaction* means any transaction involving:

(1) The sale, lease, purchase, investment in or exchange of real property, including interests in property, or the financing thereof; or

(2) The refinancing of real property or interests in real property; or

(3) The use of real property or interests in property as security for a loan or investment, including mortgage-backed securities.

(j) *State certified appraiser* means any individual who has satisfied the requirements for certification in a State

or territory whose criteria for certification as a real estate appraiser currently meet or exceed the minimum criteria for certification issued by the Appraiser Qualifications Board of the Appraisal Foundation. No individual shall be a State certified appraiser unless such individual has achieved a passing grade upon a suitable examination administered by a State or territory that is consistent with and equivalent to the Uniform State Certification Examination issued or endorsed by the Appraiser Qualifications Board of the Appraisal Foundation. In addition, the Appraisal Subcommittee must not have issued a finding that the policies, practices, or procedures of the State or territory are inconsistent with title XI of FIRREA. The Board may, from time to time, impose additional qualification criteria for certified appraisers performing appraisals in connection with federally related transactions within its jurisdiction.

(k) *State licensed appraiser* means any individual who has satisfied the requirements for licensing in a State or territory where the licensing procedures comply with title XI of FIRREA and where the Appraisal Subcommittee has not issued a finding that the policies, practices, or procedures of the State or territory are inconsistent with title XI. The Board may, from time to time, impose additional qualification criteria for licensed appraisers performing appraisals in connection with federally related transactions within the Board's jurisdiction.

(l) *Tract development* means a project of five units or more that is constructed or is to be constructed as a single development.

(m) *Transaction value* means:

(1) For loans or other extensions of credit, the amount of the loan or extension of credit;

(2) For sales, leases, purchases, and investments in or exchanges of real property, the market value of the real property interest involved; and

(3) For the pooling of loans or interests in real property for resale or purchase, the amount of the loan or the market value of the real property calculated with respect to each such loan or interest in real property.

[Reg. Y, 55 FR 27771, July 5, 1990, as amended at 59 FR 29500, June 7, 1994]

§ 225.63 Appraisals required; transactions requiring a State certified or licensed appraiser.

(a) *Appraisals required.* An appraisal performed by a State certified or licensed appraiser is required for all real estate-related financial transactions except those in which:

(1) The transaction value is $250,000 or less;

(2) A lien on real estate has been taken as collateral in an abundance of caution;

(3) The transaction is not secured by real estate;

(4) A lien on real estate has been taken for purposes other than the real estate's value;

(5) The transaction is a business loan that:

(i) Has a transaction value of $1 million or less; and

(ii) Is not dependent on the sale of, or rental income derived from, real estate as the primary source of repayment;

(6) A lease of real estate is entered into, unless the lease is the economic equivalent of a purchase or sale of the leased real estate;

(7) The transaction involves an existing extension of credit at the lending institution, provided that:

(i) There has been no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or

(ii) There is no advancement of new monies, other than funds necessary to cover reasonable closing costs;

(8) The transaction involves the purchase, sale, investment in, exchange of, or extension of credit secured by, a loan or interest in a loan, pooled loans, or interests in real property, including mortgaged-backed securities, and each loan or interest in a loan, pooled loan, or real property interest met Board regulatory requirements for appraisals at the time of origination;

(9) The transaction is wholly or partially insured or guaranteed by a

United States government agency or United States government sponsored agency;

(10) The transaction either:

(i) Qualifies for sale to a United States government agency or United States government sponsored agency; or

(ii) Involves a residential real estate transaction in which the appraisal conforms to the Federal National Mortgage Association or Federal Home Loan Mortgage Corporation appraisal standards applicable to that category of real estate;

(11) The regulated institution is acting in a fiduciary capacity and is not required to obtain an appraisal under other law;

(12) The transaction involves underwriting or dealing in mortgage-backed securities; or

(13) The Board determines that the services of an appraiser are not necessary in order to protect Federal financial and public policy interests in real estate-related financial transactions or to protect the safety and soundness of the institution.

(b) *Evaluations required.* For a transaction that does not require the services of a State certified or licensed appraiser under paragraph (a)(1), (a)(5) or (a)(7) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

(c) *Appraisals to address safety and soundness concerns.* The Board reserves the right to require an appraisal under this subpart whenever the agency believes it is necessary to address safety and soundness concerns.

(d) *Transactions requiring a State certified appraiser*—(1) *All transactions of $1,000,000 or more.* All federally related transactions having a transaction value of $1,000,000 or more shall require an appraisal prepared by a State certified appraiser.

(2) *Nonresidential transactions of $250,000 or more.* All federally related transactions having a transaction value of $250,000 or more, other than those involving appraisals of 1-to-4 family residential properties, shall require an appraisal prepared by a State certified appraiser.

(3) *Complex residential transactions of $250,000 or more.* All complex 1-to-4 family residential property appraisals rendered in connection with federally related transactions shall require a State certified appraiser if the transaction value is $250,000 or more. A regulated institution may presume that appraisals of 1-to-4 family residential properties are not complex, unless the institution has readily available information that a given appraisal will be complex. The regulated institution shall be responsible for making the final determination of whether the appraisal is complex. If during the course of the appraisal a licensed appraiser identifies factors that would result in the property, form of ownership, or market conditions being considered atypical, then either:

(i) The regulated institution may ask the licensed appraiser to complete the appraisal and have a certified appraiser approve and co-sign the appraisal; or

(ii) The institution may engage a certified appraiser to complete the appraisal.

(e) *Transactions requiring either a State certified or licensed appraiser.* All appraisals for federally related transactions not requiring the services of a State certified appraiser shall be prepared by either a State certified appraiser or a State licensed appraiser.

[Reg. Y, 55 FR 27771, July 5, 1990, as amended at 58 FR 15077, Mar. 19, 1993; 59 FR 29500, June 7, 1994; 63 FR 65532, Nov. 27, 1998]

§ 225.64 Minimum appraisal standards.

For federally related transactions, all appraisals shall, at a minimum:

(a) Conform to generally accepted appraisal standards as evidenced by the Uniform Standards of Professional Appraisal Practice promulgated by the Appraisal Standards Board of the Appraisal Foundation, 1029 Vermont Ave., NW., Washington, DC 20005, unless principles of safe and sound banking require compliance with stricter standards;

(b) Be written and contain sufficient information and analysis to support the institution's decision to engage in the transaction;

(c) Analyze and report appropriate deductions and discounts for proposed construction or renovation, partially

leased buildings, non-market lease terms, and tract developments with unsold units;

(d) Be based upon the definition of market value as set forth in this subpart; and

(e) Be performed by State licensed or certified appraisers in accordance with requirements set forth in this subpart.

[Reg. Y, 59 FR 29501, June 7, 1994]

§ 225.65 Appraiser independence.

(a) *Staff appraisers.* If an appraisal is prepared by a staff appraiser, that appraiser must be independent of the lending, investment, and collection functions and not involved, except as an appraiser, in the federally related transaction, and have no direct or indirect interest, financial or otherwise, in the property. If the only qualified persons available to perform an appraisal are involved in the lending, investment, or collection functions of the regulated institution, the regulated institution shall take appropriate steps to ensure that the appraisers exercise independent judgment and that the appraisal is adequate. Such steps include, but are not limited to, prohibiting an individual from performing appraisals in connection with federally related transactions in which the appraiser is otherwise involved and prohibiting directors and officers from participating in any vote or approval involving assets on which they performed an appraisal.

(b) *Fee appraisers.* (1) If an appraisal is prepared by a fee appraiser, the appraiser shall be engaged directly by the regulated institution or its agent, and have no direct or indirect interest, financial or otherwise, in the property or the transaction.

(2) A regulated institution also may accept an appraisal that was prepared by an appraiser engaged directly by another financial services institution, if:

(i) The appraiser has no direct or indirect interest, financial or otherwise, in the property or the transaction; and

(ii) The regulated institution determines that the appraisal conforms to the requirements of this subpart and is otherwise acceptable.

[Reg. Y, 55 FR 27771, July 5, 1990, as amended at 59 FR 29501, June 7, 1994]

§ 225.66 Professional association membership; competency.

(a) *Membership in appraisal organizations.* A State certified appraiser or a State licensed appraiser may not be excluded from consideration for an assignment for a federally related transaction solely by virtue of membership or lack of membership in any particular appraisal organization.

(b) *Competency.* All staff and fee appraisers performing appraisals in connection with federally related transactions must be State certified or licensed, as appropriate. However, a State certified or licensed appraiser may not be considered competent solely by virtue of being certified or licensed. Any determination of competency shall be based upon the individual's experience and educational background as they relate to the particular appraisal assignment for which he or she is being considered.

§ 225.67 Enforcement.

Institutions and institution-affiliated parties, including staff appraisers and fee appraisers, may be subject to removal and/or prohibition orders, cease and desist orders, and the imposition of civil money penalties pursuant to the Federal Deposit Insurance Act, 12 U.S.C 1811 *et seq.*, as amended, or other applicable law.

Subpart H—Notice of Addition or Change of Directors and Senior Executive Officers

SOURCE: Reg. Y, 62 FR 9341, Feb. 28, 1997, unless otherwise noted.

§ 225.71 Definitions.

(a) *Director* means a person who serves on the board of directors of a regulated institution, except that this term does not include an advisory director who:

(1) Is not elected by the shareholders of the regulated institution;

(2) Is not authorized to vote on any matters before the board of directors or any committee thereof;

(3) Solely provides general policy advice to the board of directors and any committee thereof; and

(4) Has not been identified by the Board or Reserve Bank as a person who performs the functions of a director for purposes of this subpart.

(b) *Regulated institution* means a state member bank or a bank holding company.

(c) *Senior executive officer* means a person who holds the title or, without regard to title, salary, or compensation, performs the function of one or more of the following positions: president, chief executive officer, chief operating officer, chief financial officer, chief lending officer, or chief investment officer. *Senior executive officer* also includes any other person identified by the Board or Reserve Bank, whether or not hired as an employee, with significant influence over, or who participates in, major policymaking decisions of the regulated institution.

(d) *Troubled condition* for a regulated institution means an institution that:

(1) Has a composite rating, as determined in its most recent report of examination or inspection, of 4 or 5 under the Uniform Financial Institutions Rating System or under the Federal Reserve Bank Holding Company Rating System;

(2) Is subject to a cease-and-desist order or formal written agreement that requires action to improve the financial condition of the institution, unless otherwise informed in writing by the Board or Reserve Bank; or

(3) Is informed in writing by the Board or Reserve Bank that it is in troubled condition for purposes of the requirements of this subpart on the basis of the institution's most recent report of condition or report of examination or inspection, or other information available to the Board or Reserve Bank.

§ 225.72 Director and officer appointments; prior notice requirement.

(a) *Prior notice by regulated institution.* A regulated institution shall give the Board 30 days' written notice, as specified in § 225.73, before adding or replacing any member of its board of directors, employing any person as a senior executive officer of the institution, or changing the responsibilities of any senior executive officer so that the person would assume a different senior executive officer position, if:

(1) The regulated institution is not in compliance with all minimum capital requirements applicable to the institution as determined on the basis of the institution's most recent report of condition or report of examination or inspection;

(2) The regulated institution is in troubled condition; or

(3) The Board determines, in connection with its review of a capital restoration plan required under section 38 of the Federal Deposit Insurance Act or subpart B of the Board's Regulation H, or otherwise, that such notice is appropriate.

(b) *Prior notice by individual.* The prior notice required by paragraph (a) of this section may be provided by an individual seeking election to the board of directors of a regulated institution.

§ 225.73 Procedures for filing, processing, and acting on notices; standards for disapproval; waiver of notice.

(a) *Filing notice*—(1) *Content.* The notice required in § 225.72 shall be filed with the appropriate Reserve Bank and shall contain:

(i) The information required by paragraph 6(A) of the Change in Bank Control Act (12 U.S.C. 1817(j)(6)(A)) as may be prescribed in the designated Board form;

(ii) Additional information consistent with the Federal Financial Institutions Examination Council's Joint Statement of Guidelines on Conducting Background Checks and Change in Control Investigations, as set forth in the designated Board form; and

(iii) Such other information as may be required by the Board or Reserve Bank.

(2) *Modification.* The Reserve Bank may modify or accept other information in place of the requirements of § 225.73(a)(1) for a notice filed under this subpart.

(3) *Acceptance and processing of notice.* The 30-day notice period specified in § 225.72 shall begin on the date all information required to be submitted by the notificant pursuant to § 225.73(a)(1) is received by the appropriate Reserve

Bank. The Reserve Bank shall notify the regulated institution or individual submitting the notice of the date on which all required information is received and the notice is accepted for processing, and of the date on which the 30-day notice period will expire. The Board or Reserve Bank may extend the 30-day notice period for an additional period of not more than 60 days by notifying the regulated institution or individual filing the notice that the period has been extended and stating the reason for not processing the notice within the 30-day notice period.

(b) *Commencement of service*—(1) *At expiration of period.* A proposed director or senior executive officer may begin service after the end of the 30-day period and any extension as provided under paragraph (a)(3) of this section, unless the Board or Reserve Bank disapproves the notice before the end of the period.

(2) *Prior to expiration of period.* A proposed director or senior executive officer may begin service before the end of the 30-day period and any extension as provided under paragraph (a)(3) of this section, if the Board or the Reserve Bank notifies in writing the regulated institution or individual submitting the notice of the Board's or Reserve Bank's intention not to disapprove the notice.

(c) *Notice of disapproval.* The Board or Reserve Bank shall disapprove a notice under § 225.72 if the Board or Reserve Bank finds that the competence, experience, character, or integrity of the individual with respect to whom the notice is submitted indicates that it would not be in the best interests of the depositors of the regulated institution or in the best interests of the public to permit the individual to be employed by, or associated with, the regulated institution. The notice of disapproval shall contain a statement of the basis for disapproval and shall be sent to the regulated institution and the disapproved individual.

(d) *Appeal of a notice of disapproval.* (1) A disapproved individual or a regulated institution that has submitted a notice that is disapproved under this section may appeal the disapproval to the Board within 15 days of the effective date of the notice of disapproval. An appeal shall be in writing and explain the reasons for the appeal and include all facts, documents, and arguments that the appealing party wishes to be considered in the appeal, and state whether the appealing party is requesting an informal hearing.

(2) Written notice of the final decision of the Board shall be sent to the appealing party within 60 days of the receipt of an appeal, unless the appealing party's request for an informal hearing is granted.

(3) The disapproved individual may not serve as a director or senior executive officer of the state member bank or bank holding company while the appeal is pending.

(e) *Informal hearing.* (1) An individual or regulated institution whose notice under this section has been disapproved may request an informal hearing on the notice. A request for an informal hearing shall be in writing and shall be submitted within 15 days of a notice of disapproval. The Board may, in its sole discretion, order an informal hearing if the Board finds that oral argument is appropriate or necessary to resolve disputes regarding material issues of fact.

(2) An informal hearing shall be held within 30 days of a request, if granted, unless the requesting party agrees to a later date.

(3) Written notice of the final decision of the Board shall be given to the individual and the regulated institution within 60 days of the conclusion of any informal hearing ordered by the Board, unless the requesting party agrees to a later date.

(f) *Waiver of notice*—(1) *Waiver requests.* The Board or Reserve Bank may permit an individual to serve as a senior executive officer or director before the notice required under this subpart is provided, if the Board or Reserve Bank finds that:

(i) Delay would threaten the safety or soundness of the regulated institution or a bank controlled by a bank holding company;

(ii) Delay would not be in the public interest; or

(iii) Other extraordinary circumstances exist that justify waiver of prior notice.

(2) *Automatic waiver.* An individual may serve as a director upon election

to the board of directors of a regulated institution before the notice required under this subpart is provided if the individual:

(i) Is not proposed by the management of the regulated institution;

(ii) Is elected as a new member of the board of directors at a meeting of the regulated institution; and

(iii) Provides to the appropriate Reserve Bank all the information required in §225.73(a) within two (2) business days after the individual's election.

(3) *Effect on disapproval authority.* A waiver shall not affect the authority of the Board or Reserve Bank to disapprove a notice within 30 days after a waiver is granted under paragraph (f)(1) of this section or the election of an individual who has filed a notice and is serving pursuant to an automatic waiver under paragraph (f)(2) of this section.

Subpart I—Financial Holding Companies

SOURCE: Reg. Y, 66 FR 415, Jan. 3, 2001, unless otherwise noted.

§225.81 What is a financial holding company?

(a) *Definition.* A financial holding company is a bank holding company that meets the requirements of this section.

(b) *Requirements to be a financial holding company.* In order to be a financial holding company:

(1) All depository institutions controlled by the bank holding company must be and remain well capitalized;

(2) All depository institutions controlled by the bank holding company must be and remain well managed; and

(3) The bank holding company must have made an effective election to become a financial holding company.

(c) *Requirements for foreign banks that are or are owned by bank holding companies*—(1) *Foreign banks with U.S. branches or agencies that also own U.S. banks.* A foreign bank that is a bank holding company and that operates a branch or agency or owns or controls a commercial lending company in the United States must comply with the requirements of this section, §225.82, and §§225.90 through 225.92 in order to be a financial holding company. After it becomes a financial holding company, a foreign bank described in this paragraph will be subject to the provisions of §§225.83, 225.84, 225.93, and 225.94.

(2) *Bank holding companies that own foreign banks with U.S. branches or agencies.* A bank holding company that owns a foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States must comply with the requirements of this section, §225.82, and §§225.90 through 225.92 in order to be a financial holding company. After it becomes a financial holding company, a bank holding company described in this paragraph will be subject to the provisions of §§225.83, 225.84, 225.93, and 225.94.

§225.82 How does a bank holding company elect to become a financial holding company?

(a) *Filing requirement.* A bank holding company may elect to become a financial holding company by filing a written declaration with the appropriate Reserve Bank. A declaration by a bank holding company is considered to be filed on the date that all information required by paragraph (b) of this section is received by the appropriate Reserve Bank.

(b) *Contents of declaration.* To be deemed complete, a declaration must:

(1) State that the bank holding company elects to be a financial holding company;

(2) Provide the name and head office address of the bank holding company and of each depository institution controlled by the bank holding company;

(3) Certify that each depository institution controlled by the bank holding company is well capitalized as of the date the bank holding company submits its declaration;

(4) Provide the capital ratios as of the close of the previous quarter for all relevant capital measures, as defined in section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o), for each depository institution controlled by the company on the date the company submits its declaration; and

(5) Certify that each depository institution controlled by the company is well managed as of the date the company submits its declaration.

(c) *Effectiveness of election.* An election by a bank holding company to become a financial holding company shall not be effective if, during the period provided in paragraph (e) of this section, the Board finds that, as of the date the declaration was filed with the appropriate Reserve Bank:

(1) Any insured depository institution controlled by the bank holding company (except an institution excluded under paragraph (d) of this section) has not achieved at least a rating of ''satisfactory record of meeting community credit needs'' under the Community Reinvestment Act at the institution's most recent examination; or

(2) Any depository institution controlled by the bank holding company is not both well capitalized and well managed.

(d) *Consideration of the CRA performance of a recently acquired insured depository institution.* Except as provided in paragraph (f) of this section, an insured depository institution will be excluded for purposes of the review of the Community Reinvestment Act rating provisions of paragraph (c)(1) of this section if:

(1) The bank holding company acquired the insured depository institution during the 12-month period preceding the filing of an election under paragraph (a) of this section;

(2) The bank holding company has submitted an affirmative plan to the appropriate Federal banking agency for the institution to take actions necessary for the institution to achieve at least a rating of ''satisfactory record of meeting community credit needs'' under the Community Reinvestment Act at the next examination of the institution; and

(3) The appropriate Federal banking agency for the institution has accepted the plan described in paragraph (d)(2) of this section.

(e) *Effective date of election*—(1) *In general.* An election filed by a bank holding company under paragraph (a) of this section is effective on the 31st calendar day after the date that a complete declaration was filed with the appropriate Reserve Bank, unless the Board notifies the bank holding company prior to that time that the election is ineffective.

(2) *Earlier notification that an election is effective.* The Board or the appropriate Reserve Bank may notify a bank holding company that its election to become a financial holding company is effective prior to the 31st day after the date that a complete declaration was filed with the appropriate Reserve Bank. Such a notification must be in writing.

(f) *Requests to become a financial holding company submitted as part of an application to become a bank holding company*—(1) *In general.* A company that is not a bank holding company and has applied for the Board's approval to become a bank holding company under section 3(a)(1) of the BHC Act (12 U.S.C. 1842(a)(1)) may as part of that application submit a request to become a financial holding company.

(2) *Contents of request.* A request to become a financial holding company submitted as part of an application to become a bank holding company must:

(i) State that the company seeks to become a financial holding company on consummation of its proposal to become a bank holding company; and

(ii) Certify that each depository institution that would be controlled by the company on consummation of its proposal to become a bank holding company will be both well capitalized and well managed as of the date the company consummates the proposal.

(3) *Request becomes a declaration and an effective election on date of consummation of bank holding company proposal.* A complete request submitted by a company under this paragraph (f) becomes a complete declaration by a bank holding company for purposes of section 4(l) of the BHC Act (12 U.S.C. 1843(l)) and becomes an effective election for purposes of § 225.81(b) on the date that the company lawfully consummates its proposal under section 3 of the BHC Act (12 U.S.C. 1842), unless the Board notifies the company at any time prior to consummation of the proposal and that:

(i) Any depository institution that would be controlled by the company on consummation of the proposal will not

be both well capitalized and well managed on the date of consummation; or

(ii) Any insured depository institution that would be controlled by the company on consummation of the proposal has not achieved at least a rating of ''satisfactory record of meeting community credit needs'' under the Community Reinvestment Act at the institution's most recent examination.

(4) *Limited exclusion for recently acquired institutions not available.* Unless the Board determines otherwise, an insured depository institution that is controlled or would be controlled by the company as part of its proposal to become a bank holding company may not be excluded for purposes of evaluating the Community Reinvestment Act criterion described in this paragraph or in paragraph (d) of this section.

(g) *Board's authority to exercise supervisory authority over a financial holding company.* An effective election to become a financial holding company does not in any way limit the Board's statutory authority under the BHC Act, the Federal Deposit Insurance Act, or any other relevant Federal statute to take appropriate action, including imposing supervisory limitations, restrictions, or prohibitions on the activities and acquisitions of a bank holding company that has elected to become a financial holding company, or enforcing compliance with applicable law.

§ 225.83 What are the consequences of failing to continue to meet applicable capital and management requirements?

(a) *Notice by the Board.* If the Board finds that a financial holding company controls any depository institution that is not well capitalized or well managed, the Board will notify the company in writing that it is not in compliance with the applicable requirement(s) for a financial holding company and identify the area(s) of noncompliance. The Board may provide this notice at any time before or after receiving notice from the financial holding company under paragraph (b) of this section.

(b) *Notification by a financial holding company required*—(1) *Notice to Board.* A financial holding company must notify the Board in writing within 15 calendar days of becoming aware that any depository institution controlled by the company has ceased to be well capitalized or well managed. This notification must identify the depository institution involved and the area(s) of noncompliance.

(2) *Triggering events for notice to the Board*—(i) *Well capitalized.* A company becomes aware that a depository institution it controls is no longer well capitalized upon the occurrence of any material event that would change the category assigned to the institution for purposes of section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o). *See* 12 CFR 6.3(b)–(c), 208.42(b)–(c), and 325.102(b)–(c).

(ii) *Well managed.* A company becomes aware that a depository institution it controls is no longer well managed at the time the depository institution receives written notice from the appropriate Federal or state banking agency that either its composite rating or its rating for management is not at least satisfactory.

(c) *Execution of agreement acceptable to the Board*—(1) *Agreement required; time period.* Within 45 days after receiving a notice from the Board under paragraph (a) of this section, the company must execute an agreement acceptable to the Board to comply with all applicable capital and management requirements.

(2) *Extension of time for executing agreement.* Upon request by a company, the Board may extend the 45-day period under paragraph (c)(1) of this section if the Board determines that granting additional time is appropriate under the circumstances. A request by a company for additional time must include an explanation of why an extension is necessary.

(3) *Agreement requirements.* An agreement required by paragraph (c)(1) of this section to correct a capital or management deficiency must:

(i) Explain the specific actions that the company will take to correct all areas of noncompliance;

(ii) Provide a schedule within which each action will be taken;

(iii) Provide any other information that the Board may require; and

(iv) Be acceptable to the Board.

(d) *Limitations during period of noncompliance*—Until the Board determines that a company has corrected the conditions described in a notice under paragraph (a) of this section:

(1) The Board may impose any limitations or conditions on the conduct or activities of the company or any of its affiliates as the Board finds to be appropriate and consistent with the purposes of the BHC Act; and

(2) The company and its affiliates may not commence any additional activity or acquire control or shares of any company under section 4(k) of the BHC Act without prior approval from the Board.

(e) *Consequences of failure to correct conditions within 180 days*—(1) *Divestiture of depository institutions.* If a company does not correct the conditions described in a notice under paragraph (a) of this section within 180 days of receipt of the notice or such additional time as the Board may permit, the Board may order the company to divest ownership or control of any depository institution owned or controlled by the company. Such divestiture must be done in accordance with the terms and conditions established by the Board.

(2) *Alternative method of complying with a divestiture order.* A company may comply with an order issued under paragraph (e)(1) of this section by ceasing to engage (both directly and through any subsidiary that is not a depository institution or a subsidiary of a depository institution) in any activity that may be conducted only under section 4(k), (n), or (o) of the BHC Act (12 U.S.C. 1843(k), (n), or (o)). The termination of activities must be completed within the time period referred to in paragraph (e)(1) of this section and in accordance with the terms and conditions acceptable to the Board.

(f) *Consultation with other agencies.* In taking any action under this section, the Board will consult with the relevant Federal and state regulatory authorities.

§ 225.84 What are the consequences of failing to maintain a satisfactory or better rating under the Community Reinvestment Act at all insured depository institution subsidiaries?

(a) *Limitations on activities*—(1) *In general.* Upon receiving a notice regarding performance under the Community Reinvestment Act in accordance with paragraph (a)(2) of this section, a financial holding company may not:

(i) Commence any additional activity under section 4(k) or 4(n) of the BHC Act (12 U.S.C. 1843(k) or (n)); or

(ii) Directly or indirectly acquire control, including all or substantially all of the assets, of a company engaged in any activity under section 4(k) or 4(n) of the BHC Act (12 U.S.C. 1843(k) or (n)).

(2) *Notification.* A financial holding company receives notice for purposes of this paragraph at the time that the appropriate Federal banking agency for any insured depository institution controlled by the company or the Board provides notice to the institution or company that the institution has received a rating of ''needs to improve record of meeting community credit needs'' or ''substantial noncompliance in meeting community credit needs'' in the institution's most recent examination under the Community Reinvestment Act.

(b) *Exceptions for certain activities*—(1) *Continuation of investment activities.* The prohibition in paragraph (a) of this section does not prevent a financial holding company from continuing to make investments in the ordinary course of conducting merchant banking activities under section 4(k)(4)(H) of the BHC Act (12 U.S.C. 1843(k)(4)(H)) or insurance company investment activities under section 4(k)(4)(I) of the BHC Act (12 U.S.C. 1843(k)(4)(I))if:

(i) The financial holding company lawfully was a financial holding company and commenced the merchant banking activity under section 4(k)(4)(H) of the BHC Act (12 U.S.C. 1843(k)(4)(H)) or the insurance company investment activity under section 4(k)(4)(I) of the BHC Act (12 U.S.C. 1843(k)(4)(I)) prior to the time that an insured depository institution controlled by the financial holding company received a rating below ''satisfactory record of meeting community credit needs'' under the Community Reinvestment Act; and

(ii) The Board has not, in the exercise of its supervisory authority, advised the financial holding company that these activities must be restricted.

(2) *Activities that are closely related to banking.* The prohibition in paragraph (a) of this section does not prevent a financial holding company from commencing any additional activity or acquiring control of a company engaged in any activity under section 4(c) of the BHC Act (12 U.S.C. 1843(c)), if the company complies with the notice, approval, and other requirements of that section and section 4(j) of the BHC Act (12 U.S.C. 1843(j)).

(c) *Duration of prohibitions.* The prohibitions described in paragraph (a) of this section shall continue in effect until such time as each insured depository institution controlled by the financial holding company has achieved at least a rating of ''satisfactory record of meeting community credit needs'' under the Community Reinvestment Act at the most recent examination of the institution.

§ 225.85 Is notice to or approval from the Board required prior to engaging in a financial activity?

(a) *No prior approval required generally*—(1) *In general.* A financial holding company and any subsidiary (other than a depository institution or subsidiary of a depository institution) of the financial holding company may engage in any activity listed in § 225.86, or acquire shares or control of a company engaged exclusively in activities listed in § 225.86, without providing prior notice to or obtaining prior approval from the Board unless required under paragraph (c) of this section.

(2) *Acquisitions by a financial holding company of a company engaged in other permissible activities.* In addition to the activities listed in § 225.86, a company acquired or to be acquired by a financial holding company under paragraph (a)(1) of this section may engage in activities otherwise permissible for a financial holding company under this part in accordance with any applicable notice, approval, or other requirement.

(3) *Acquisition by a financial holding company of a company engaged in limited nonfinancial activities*—(i) *Mixed acquisitions generally permitted.* A financial holding company may under this subpart acquire more than 5 percent of the outstanding shares of any class of voting securities or control of a company that is not engaged exclusively in activities that are financial in nature, incidental to a financial activity, or otherwise permissible for the financial holding company under section 4(c) of the BHC Act (12 U.S.C. 1843(c)) if:

(A) The company to be acquired is substantially engaged in activities that are financial in nature, incidental to a financial activity, or otherwise permissible for the financial holding company under section 4(c) of the BHC Act (12 U.S.C. 1843(c));

(B) The financial holding company complies with the notice requirements of § 225.87, if applicable; and

(C) The company conforms, terminates, or divests, within 2 years of the date the financial holding company acquires shares or control of the company, all activities that are not financial in nature, incidental to a financial activity, or otherwise permissible for the financial holding company under section 4(c) (12 U.S.C. 1843(c))of the BHC Act.

(ii) *Definition of ''substantially engaged.''* Unless the Board determines otherwise, a company will be considered to be ''substantially engaged'' in activities permissible for a financial holding company for purposes of paragraph (a)(3)(A) of this section if at least 85 percent of the company's consolidated total annual gross revenues is derived from and at least 85 percent of the company's consolidated total assets is attributable to the conduct of activities that are financial in nature, incidental to a financial activity, or otherwise permissible for a financial holding company under section 4(c) of the BHC Act (12 U.S.C. 1843(c)).

(b) *Locations in which a financial holding company may conduct financial activities.* A financial holding company may conduct any activity listed in § 225.86 at any location in the United States or at any location outside of the United States subject to the laws of the jurisdiction in which the activity is conducted.

(c) *Circumstances under which prior notice to the Board is required*—(1) *Acquisition of more than 5 percent of the shares of a savings association.* A financial holding company must obtain Board approval in accordance with section 4(j) of the BHC Act (12 U.S.C. 1843(j))

and either § 225.14 or § 225.24, as appropriate, prior to acquiring control or more than 5 percent of the outstanding shares of any class of voting securities of a savings association or of a company that owns, operates, or controls a savings association.

(2) *Supervisory actions.* The Board may, if appropriate in the exercise of its supervisory or other authority, including under § 225.82(g) or § 225.83(d) or other relevant authority, require a financial holding company to provide notice to or obtain approval from the Board prior to engaging in any activity or acquiring shares or control of any company.

§ 225.86 What activities are permissible for any financial holding company?

The following activities are financial in nature or incidental to a financial activity:

(a) *Activities determined to be closely related to banking.* (1) Any activity that the Board had determined by regulation prior to November 12, 1999, to be so closely related to banking as to be a proper incident thereto, subject to the terms and conditions contained in this part, unless modified by the Board. These activities are listed in § 225.28.

(2) Any activity that the Board had determined by an order that was in effect on November 12, 1999, to be so closely related to banking as to be a proper incident thereto, subject to the terms and conditions contained in this part and those in the authorizing orders. These activities are:

(i) Providing administrative and other services to mutual funds (*Societe Generale*, 84 Federal Reserve Bulletin 680 (1998));

(ii) Owning shares of a securities exchange (*J.P. Morgan & Co, Inc., and UBS AG*, 86 Federal Reserve Bulletin 61 (2000));

(iii) Acting as a certification authority for digital signatures and authenticating the identity of persons conducting financial and nonfinancial transactions (*Bayerische Hypo- und Vereinsbank AG, et al.*, 86 Federal Reserve Bulletin 56 (2000));

(iv) Providing employment histories to third parties for use in making credit decisions and to depository institutions and their affiliates for use in the ordinary course of business (*Norwest Corporation*, 81 Federal Reserve Bulletin 732 (1995));

(v) Check cashing and wire transmission services (*Midland Bank, PLC*, 76 Federal Reserve Bulletin 860 (1990) (check cashing); *Norwest Corporation*, 81 Federal Reserve Bulletin 1130 (1995) (money transmission));

(vi) In connection with offering banking services, providing notary public services, selling postage stamps and postage-paid envelopes, providing vehicle registration services, and selling public transportation tickets and tokens (*Popular, Inc.*, 84 Federal Reserve Bulletin 481 (1998)); and

(vii) Real estate title abstracting (*The First National Company*, 81 Federal Reserve Bulletin 805 (1995)).

(b) *Activities determined to be usual in connection with the transaction of banking abroad.* Any activity that the Board had determined by regulation in effect on November 11, 1999, to be usual in connection with the transaction of banking or other financial operations abroad (*see* § 211.5(d) of this chapter), subject to the terms and conditions in part 211 and Board interpretations in effect on that date regarding the scope and conduct of the activity. In addition to the activities listed in paragraphs (a) and (c) of this section, these activities are:

(1) Providing management consulting services, including to any person with respect to nonfinancial matters, so long as the management consulting services are advisory and do not allow the financial holding company to control the person to which the services are provided;

(2) Operating a travel agency in connection with financial services offered by the financial holding company or others; and

(3) Organizing, sponsoring, and managing a mutual fund, so long as:

(i) The fund does not exercise managerial control over the entities in which the fund invests; and

(ii) The financial holding company reduces its ownership in the fund, if any, to less than 25 percent of the equity of the fund within one year of sponsoring the fund or such additional period as the Board permits.

(c) *Activities permitted under section 4(k)(4) of the BHC Act* (12 U.S.C. 1843(k)(4)). Any activity defined to be financial in nature under sections 4(k)(4)(A) through (E), (H) and (I) of the BHC Act (12 U.S.C. 1843(k)(4)(A) through (E), (H) and (I)).

(d) *Activities determined to be financial in nature or incidental to financial activities by the Board*—(1) *Acting as a finder*—Acting as a finder in bringing together one or more buyers and sellers of any product or service for transactions that the parties themselves negotiate and consummate.

(i) *What is the scope of finder activities?* Acting as a finder includes providing any or all of the following services through any means—

(A) Identifying potential parties, making inquiries as to interest, introducing and referring potential parties to each other, and arranging contacts between and meetings of interested parties;

(B) Conveying between interested parties expressions of interest, bids, offers, orders and confirmations relating to a transaction; and

(C) Transmitting information concerning products and services to potential parties in connection with the activities described in paragraphs (d)(1)(i)(A) and (B) of this section.

(ii) *What are some examples of finder services?* The following are examples of the services that may be provided by a finder when done in accordance with paragraphs (d)(1)(iii) and (iv) of this section. These examples are not exclusive.

(A) Hosting an electronic marketplace on the financial holding company's Internet web site by providing hypertext or similar links to the web sites of third party buyers or sellers.

(B) Hosting on the financial holding company's servers the Internet web site of—

(*1*) A buyer (or seller) that provides information concerning the buyer (or seller) and the products or services it seeks to buy (or sell) and allows sellers (or buyers) to submit expressions of interest, bids, offers, orders and confirmations relating to such products or services; or

(*2*) A government or government agency that provides information concerning the services or benefits made available by the government or government agency, assists persons in completing applications to receive such services or benefits from the government or agency, and allows persons to transmit their applications for services or benefits to the government or agency.

(C) Operating an Internet web site that allows multiple buyers and sellers to exchange information concerning the products and services that they are willing to purchase or sell, locate potential counterparties for transactions, aggregate orders for goods or services with those made by other parties, and enter into transactions between themselves.

(D) Operating a telephone call center that provides permissible finder services.

(iii) *What limitations are applicable to a financial holding company acting as a finder?* (A) A finder may act only as an intermediary between a buyer and a seller.

(B) A finder may not bind any buyer or seller to the terms of a specific transaction or negotiate the terms of a specific transaction on behalf of a buyer or seller, except that a finder may—

(*1*) Arrange for buyers to receive preferred terms from sellers so long as the terms are not negotiated as part of any individual transaction, are provided generally to customers or broad categories of customers, and are made available by the seller (and not by the financial holding company); and

(*2*) Establish rules of general applicability governing the use and operation of the finder service, including rules that—

(*i*) Govern the submission of bids and offers by buyers and sellers that use the finder service and the circumstances under which the finder service will match bids and offers submitted by buyers and sellers; and

(*ii*) Govern the manner in which buyers and sellers may bind themselves to the terms of a specific transaction.

(C) A finder may not—

(*1*) Take title to or acquire or hold an ownership interest in any product or service offered or sold through the finder service;

(*2*) Provide distribution services for physical products or services offered or sold through the finder service;

(*3*) Own or operate any real or personal property that is used for the purpose of manufacturing, storing, transporting, or assembling physical products offered or sold by third parties; or

(*4*) Own or operate any real or personal property that serves as a physical location for the physical purchase, sale or distribution of products or services offered or sold by third parties.

(D) A finder may not engage in any activity that would require the company to register or obtain a license as a real estate agent or broker under applicable law.

(iv) *What disclosures are required?* A finder must distinguish the products and services offered by the financial holding company from those offered by a third party through the finder service.

(2) [Reserved]

(e) *Activities permitted under section 4(k)(5) of the Bank Holding Company Act (12 U.S.C. 1843(k)(5)).* (1) The following types of activities are financial in nature or incidental to a financial activity when conducted pursuant to a determination by the Board under paragraph (e)(2) of this section:

(i) Lending, exchanging, transferring, investing for others, or safeguarding financial assets other than money or securities;

(ii) Providing any device or other instrumentality for transferring money or other financial assets; and

(iii) Arranging, effecting, or facilitating financial transactions for the account of third parties.

(2) *Review of specific activities*—(i) *Is a specific request required?* A financial holding company that wishes to engage on the basis of paragraph (e)(1) of this section in an activity that is not otherwise permissible for a financial holding company must obtain a determination from the Board that the activity is permitted under paragraph (e)(1).

(ii) *Consultation with the Secretary of the Treasury*. After receiving a request under this section, the Board will provide the Secretary of the Treasury with a copy of the request and consult with the Secretary in accordance with section 4(k)(2)(A) of the Bank Holding Company Act (12 U.S.C. 1843(k)(2)(A)).

(iii) *Board action on requests.* After consultation with the Secretary, the Board will promptly make a written determination regarding whether the specific activity described in the request is included in an activity category listed in paragraph (e)(1) of this section and is therefore either financial in nature or incidental to a financial activity.

(3) *What factors will the Board consider?* In evaluating a request made under this section, the Board will take into account the factors listed in section 4(k)(3) of the BHC Act (12 U.S.C. 1843(k)(3)) that it must consider when determining whether an activity is financial in nature or incidental to a financial activity.

(4) *What information must the request contain?* Any request by a financial holding company under this section must be in writing and must:

(i) Identify and define the activity for which the determination is sought, specifically describing what the activity would involve and how the activity would be conducted; and

(ii) Provide information supporting the requested determination, including information regarding how the proposed activity falls into one of the categories listed in paragraph (e)(1) of this section, and any other information required by the Board concerning the proposed activity.

[Reg. Y, 66 FR 415, Jan. 3, 2001, as amended at 66 FR 19081, Apr. 13, 2001]

§ 225.87 Is notice to the Board required after engaging in a financial activity?

(a) *Post-transaction notice generally required to engage in a financial activity*. A financial holding company that commences an activity or acquires shares of a company engaged in an activity listed in § 225.86 must notify the appropriate Reserve Bank in writing within 30 calendar days after commencing the activity or consummating the acquisition by using the appropriate form.

(b) *Cases in which notice to the Board is not required*—(1) *Acquisitions that do not involve control of a company*. A notice under paragraph (a) of this section is not required in connection with the

acquisition of shares of a company if, following the acquisition, the financial holding company does not control the company.

(2) *No additional notice required to engage de novo* in an activity for which a financial holding company already has provided notice. After a financial holding company provides the appropriate Reserve Bank with notice that the company is engaged in an activity listed in §225.86, a financial holding company may, unless otherwise notified by the Board, commence the activity *de novo* through any subsidiary that the financial holding company is authorized to control without providing additional notice under paragraph (a) of this section.

(3) *Conduct of certain investment activities.* Unless required by paragraph (b)(4) of this section, a financial holding company is not required to provide notice under paragraph (a) of this section of any individual acquisition of shares of a company as part of the conduct by a financial holding company of securities underwriting, dealing, or market making activities as described in section 4(k)(4)(E) of the BHC Act (12 U.S.C. 1843(k)(4)(E)), merchant banking activities conducted pursuant to section 4(k)(4)(H) of the BHC Act (12 U.S.C. 1843(k)(4)(H)), or insurance company investment activities conducted pursuant to section 4(k)(4)(I) of the BHC Act (12 U.S.C. 1843(k)(4)(I)), if the financial holding company previously has notified the Board under paragraph (a) of this section that the company has commenced the relevant securities, merchant banking, or insurance company investment activities, as relevant.

(4) *Notice of large merchant banking or insurance company investments.* Notwithstanding paragraph (b)(1) or (b)(3) of this section, a financial holding company must provide notice under paragraph (a) of the section if:

(i) As part of a merchant banking activity conducted under section 4(k)(4)(H) of the BHC Act (12 U.S.C. 1843(k)(4)(H)), the financial holding company acquires more than 5 percent of the shares, assets, or ownership interests of any company at a total cost that exceeds the lesser of 5 percent of the financial holding company's Tier 1 capital or $200 million;

(ii) As part of an insurance company investment activity conducted under section 4(k)(4)(I) of the BHC Act (12 U.S.C. 1843(k)(4)(I)), the financial holding company acquires more than 5 percent of the shares, assets, or ownership interests of any company at a total cost that exceeds the lesser of 5 percent of the financial holding company's Tier 1 capital or $200 million; or

(iii) The Board in the exercise of its supervisory authority notifies the financial holding company that a notice is necessary.

§225.88 How to request the Board to determine that an activity is financial in nature or incidental to a financial activity?

(a) *Requests regarding activities that may be financial in nature or incidental to a financial activity.* A financial holding company or other interested party may request a determination from the Board that an activity not listed in §225.86 is financial in nature or incidental to a financial activity.

(b) *Required information.* A request submitted under this section must be in writing and must:

(1) Identify and define the activity for which the determination is sought, specifically describing what the activity would involve and how the activity would be conducted;

(2) Explain in detail why the activity should be considered financial in nature or incidental to a financial activity; and

(3) Provide information supporting the requested determination and any other information required by the Board concerning the proposed activity.

(c) *Board procedures for reviewing requests*—(1) *Consultation with the Secretary of the Treasury.* Upon receipt of the request, the Board will provide the Secretary of the Treasury a copy of the request and consult with the Secretary in accordance with section 4(k)(2)(A) of the BHC Act (12 U.S.C. 1843(k)(2)(A)).

(2) *Public notice.* The Board may, as appropriate and after consultation with the Secretary, publish a description of the proposal in the FEDERAL

REGISTER with a request for public comment.

(d) *Board action.* The Board will endeavor to make a decision on any request filed under paragraph (a) of this section within 60 calendar days following the completion of both the consultative process described in paragraph (c)(1) of this section and the public comment period, if any.

(e) *Advisory opinions regarding scope of financial activities*—(1) *Written request.* A financial holding company or other interested party may request an advisory opinion from the Board about whether a specific proposed activity falls within the scope of an activity listed in § 225.86 as financial in nature or incidental to a financial activity. The request must be submitted in writing and must contain:

(i) A detailed description of the particular activity in which the company proposes to engage or the product or service the company proposes to provide;

(ii) An explanation supporting an interpretation regarding the scope of the permissible financial activity; and

(iii) Any additional information requested by the Board regarding the activity.

(2) *Board response.* The Board will provide an advisory opinion within 45 calendar days of receiving a complete written request under paragraph (e)(1) of this section.

§ 225.89 How to request approval to engage in an activity that is complementary to a financial activity?

(a) *Prior Board approval is required.* A financial holding company that seeks to engage in or acquire more than 5 percent of the outstanding shares of any class of voting securities of a company engaged in an activity that the financial holding company believes is complementary to a financial activity must obtain prior approval from the Board in accordance with section 4(j) of the BHC Act (12 U.S.C. 1843(j)). The notice must be in writing and must:

(1) Identify and define the proposed complementary activity, specifically describing what the activity would involve and how the activity would be conducted;

(2) Identify the financial activity for which the proposed activity would be complementary and provide detailed information sufficient to support a finding that the proposed activity should be considered complementary to the identified financial activity;

(3) Describe the scope and relative size of the proposed activity, as measured by the percentage of the projected financial holding company revenues expected to be derived from and assets associated with conducting the activity;

(4) Discuss the risks that conducting the activity may reasonably be expected to pose to the safety and soundness of the subsidiary depository institutions of the financial holding company and to the financial system generally;

(5) Describe the potential adverse effects, including potential conflicts of interest, decreased or unfair competition, or other risks, that conducting the activity could raise, and explain the measures the financial holding company proposes to take to address those potential effects;

(6) Describe the potential benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that the proposal reasonably can be expected to produce; and

(7) Provide any information about the financial and managerial resources of the financial holding company and any other information requested by the Board.

(b) *Factors for consideration by the Board.* In evaluating a notice to engage in a complementary activity, the Board must consider whether:

(1) The proposed activity is complementary to a financial activity;

(2) The proposed activity would pose a substantial risk to the safety or soundness of depository institutions or the financial system generally; and

(3) The proposal could be expected to produce benefits to the public that outweigh possible adverse effects.

(c) *Board action.* The Board will inform the financial holding company in writing of the Board's determination regarding the proposed activity within the period described in section 4(j) of the BHC Act (12 U.S.C. 1843(j)).

§ 225.90 What are the requirements for a foreign bank to be treated as a financial holding company?

(a) *Foreign banks as financial holding companies.* A foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States, and any company that owns or controls such a foreign bank, will be treated as a financial holding company if:

(1) The foreign bank, any other foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, and any U.S. depository institution subsidiary that is owned or controlled by the foreign bank or company, is and remains well capitalized and well managed; and

(2) The foreign bank, and any company that owns or controls the foreign bank, has made an effective election to be treated as a financial holding company under this subpart.

(b) *Standards for ''well capitalized.''* A foreign bank will be considered ''well capitalized'' if either:

(1)(i) Its home country supervisor, as defined in §211.21 of the Board's Regulation K (12 CFR 211.21), has adopted risk-based capital standards consistent with the Capital Accord of the Basel Committee on Banking Supervision (Basel Accord);

(ii) The foreign bank maintains a Tier 1 capital to total risk-based assets ratio of 6 percent and a total capital to total risk-based assets ratio of 10 percent, as calculated under its home country standard; and

(iii) The foreign bank's capital is comparable to the capital required for a U.S. bank owned by a financial holding company; or

(2) The foreign bank has obtained a determination from the Board under §225.91(c) that the foreign bank's capital is otherwise comparable to the capital that would be required of a U.S. bank owned by a financial holding company.

(c) *Standards for ''well managed.''* A foreign bank will be considered ''well managed'' if:

(1) The foreign bank has received at least a satisfactory composite rating of its U.S. branch, agency, and commercial lending company operations at its most recent assessment;

(2) The home country supervisor of the foreign bank consents to the foreign bank expanding its activities in the United States to include activities permissible for a financial holding company; and

(3) The management of the foreign bank meets standards comparable to those required of a U.S. bank owned by a financial holding company.

§ 225.91 How may a foreign bank elect to be treated as a financial holding company?

(a) *Filing requirement.* A foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States, or a company that owns or controls such a foreign bank, may elect to be treated as a financial holding company by filing a written declaration with the appropriate Reserve Bank.

(b) *Contents of declaration.* The declaration must:

(1) State that the foreign bank or the company elects to be treated as a financial holding company;

(2) Provide the risk-based capital ratios and amount of Tier 1 capital and total assets of the foreign bank, and of each foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, as of the close of the most recent quarter and as of the close of the most recent audited reporting period;

(3) Certify that the foreign bank, and each foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, meets the standards of well capitalized set out in §225.90(b)(1)(i) and (ii) or §225.90(b)(2) as of the date the foreign bank or company files its election;

(4) Certify that the foreign bank, and each foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, is well managed as defined in §225.90(c)(1) as of the date the foreign bank or company files its election;

(5) Certify that all U.S. depository institution subsidiaries of the foreign

bank or company are well capitalized and well managed as of the date the foreign bank or company files its election; and

(6) Provide the capital ratios for all relevant capital measures (as defined in section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831(o))) as of the close of the previous quarter for each U.S. depository institution subsidiary of the foreign bank or company.

(c) *Pre-clearance process.* Before filing an election to be treated as a financial holding company, a foreign bank or company may file a request for review of its qualifications to be treated as a financial holding company. The Board will endeavor to make a determination on such requests within 30 days of receipt. A foreign bank that has not been found, or that is chartered in a country where no bank from that country has been found, by the Board under the Bank Holding Company Act or the International Banking Act to be subject to comprehensive supervision or regulation on a consolidated basis by its home country supervisor is required to use this process.

§ 225.92 How does an election by a foreign bank become effective?

(a) *In general.* An election described in § 225.91 is effective on the 31st day after the date that an election was received by the appropriate Federal Reserve Bank, unless the Board notifies the foreign bank or company prior to that time that:

(1) The election is ineffective; or

(2) The period is extended with the consent of the foreign bank or company making the election.

(b) *Earlier notification that an election is effective.* The Board or the appropriate Federal Reserve Bank may notify a foreign bank or company that its election to be treated as a financial holding company is effective prior to the 31st day after the election was filed with the appropriate Federal Reserve Bank. Such notification must be in writing.

(c) *Under what circumstances will the Board find an election to be ineffective?* An election to be treated as a financial holding company shall not be effective if, during the period provided in paragraph (a) of this section, the Board finds that:

(1) The foreign bank certificant, or any foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States and is controlled by a foreign bank or company certificant, is not both well capitalized and well managed;

(2) Any U.S. insured depository institution subsidiary of the foreign bank or company (except an institution excluded under paragraph (d) of this section) or any U.S. branch of a foreign bank that is insured by the Federal Deposit Insurance Corporation has not achieved at least a rating of ''satisfactory record of meeting community needs'' under the Community Reinvestment Act at the institution's most recent examination;

(3) Any U.S. depository institution subsidiary of the foreign bank or company is not both well capitalized and well managed; or

(4) The Board does not have sufficient information to assess whether the foreign bank or company making the election meets the requirements of this subpart.

(d) *How is CRA performance of recently acquired insured depository institutions considered?* An insured depository institution will be excluded for purposes of the review of CRA ratings described in paragraph (c)(2) of this section consistent with the provisions of § 225.82(d).

(e) *Factors used in the Board's determination regarding comparability of capital and management.*—(1) *In general.* In determining whether a foreign bank is well capitalized and well managed in accordance with comparable capital and management standards, the Board will give due regard to national treatment and equality of competitive opportunity. In this regard, the Board may take into account the foreign bank's composition of capital, Tier 1 capital to total assets leverage ratio, accounting standards, long-term debt ratings, reliance on government support to meet capital requirements, the foreign bank's anti-money laundering procedures, whether the foreign bank is subject to comprehensive supervision or regulation on a consolidated basis,

and other factors that may affect analysis of capital and management. The Board will consult with the home country supervisor for the foreign bank as appropriate.

(2) *Assessment of consolidated supervision.* A foreign bank that is not subject to comprehensive supervision on a consolidated basis by its home country authorities may not be considered well capitalized and well managed unless:

(i) The home country has made significant progress in establishing arrangements for comprehensive supervision on a consolidated basis; and

(ii) The foreign bank is in strong financial condition as demonstrated, for example, by capital levels that significantly exceed the minimum levels that are required for a well capitalized determination and strong asset quality.

§ 225.93 What are the consequences of a foreign bank failing to continue to meet applicable capital and management requirements?

(a) *Notice by the Board.* If a foreign bank or company has made an effective election to be treated as a financial holding company under this subpart and the Board finds that the foreign bank, any foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, or any U.S. depository institution subsidiary controlled by the foreign bank or company, ceases to be well capitalized or well managed, the Board will notify the foreign bank and company, if any, in writing that it is not in compliance with the applicable requirement(s) for a financial holding company and identify the areas of noncompliance.

(b) *Notification by a financial holding company required.*—(1) *Notice to Board.* Promptly upon becoming aware that the foreign bank, any foreign bank that maintains a U.S. branch, agency, or commercial lending company and is controlled by the foreign bank or company, or any U.S. depository institution subsidiary of the foreign bank or company, has ceased to be well capitalized or well managed, the foreign bank and company, if any, must notify the Board and identify the area of noncompliance.

(2) *Triggering events for notice to the Board*—(i) *Well capitalized.* A foreign bank becomes aware that it is no longer well capitalized at the time that the foreign bank or company is required to file a report of condition (or similar supervisory report) with its home country supervisor or the appropriate Federal Reserve Bank that indicates that the foreign bank no longer meets the well capitalized standards.

(ii) *Well managed.* A foreign bank becomes aware that it is no longer well managed at the time that the foreign bank receives written notice from the appropriate Federal Reserve Bank that the composite rating of its U.S. branch, agency, and commercial lending company operations is not at least satisfactory.

(c) *Execution of agreement acceptable to the Board*—(1) *Agreement required; time period.* Within 45 days after receiving a notice under paragraph (a) of this section, the foreign bank or company must execute an agreement acceptable to the Board to comply with all applicable capital and management requirements.

(2) *Extension of time for executing agreement.* Upon request by the foreign bank or company, the Board may extend the 45-day period under paragraph (c)(1) of this section if the Board determines that granting additional time is appropriate under the circumstances. A request by a foreign bank or company for additional time must include an explanation of why an extension is necessary.

(3) *Agreement requirements.* An agreement required by paragraph (c)(1) of this section to correct a capital or management deficiency must:

(i) Explain the specific actions that the foreign bank or company will take to correct all areas of noncompliance;

(ii) Provide a schedule within which each action will be taken;

(iii) Provide any other information that the Board may require; and

(iv) Be acceptable to the Board.

(d) *Limitations during period of noncompliance*—Until the Board determines that a foreign bank or company has corrected the conditions described in a notice under paragraph (a) of this section:

(1) The Board may impose any limitations or conditions on the conduct or the U.S. activities of the foreign bank or company or any of its affiliates as the Board finds to be appropriate and consistent with the purposes of the Bank Holding Company Act; and

(2) The foreign bank or company and its affiliates may not commence any additional activity in the United States or acquire control or shares of any company under section 4(k) of the Bank Holding Company Act (12 U.S.C. 1843(k)) without prior approval from the Board.

(e) *Consequences of failure to correct conditions within 180 days*—(1) *Termination of Offices and Divestiture.* If a foreign bank or company does not correct the conditions described in a notice under paragraph (a) of this section within 180 days of receipt of the notice or such additional time as the Board may permit, the Board may order the foreign bank or company to terminate the foreign bank's U.S. branches and agencies and divest any commercial lending companies owned or controlled by the foreign bank or company. Such divestiture must be done in accordance with the terms and conditions established by the Board.

(2) *Alternative method of complying with a divestiture order.* A foreign bank or company may comply with an order issued under paragraph (e)(1) of this section by ceasing to engage (both directly and through any subsidiary that is not a depository institution or a subsidiary of a depository institution) in any activity that may be conducted only under section 4(k), (n), or (o) of the BHC Act (12 U.S.C. 1843(k), (n) and (o)). The termination of activities must be completed within the time period referred to in paragraph (e)(1) of this section and subject to terms and conditions acceptable to the Board.

(f) *Consultation with Other Agencies.* In taking any action under this section, the Board will consult with the relevant Federal and state regulatory authorities and the appropriate home country supervisor(s) of the foreign bank.

§ 225.94 What are the consequences of an insured branch or depository institution failing to maintain a satisfactory or better rating under the Community Reinvestment Act?

(a) *Insured branch as an ''insured depository institution.''* A U.S. branch of a foreign bank that is insured by the Federal Deposit Insurance Corporation shall be treated as an ''insured depository institution'' for purposes of § 225.84.

(b) *Applicability.* The provisions of § 225.84, with the modifications contained in this section, shall apply to a foreign bank that operates an insured branch referred to in paragraph (a) of this section or an insured depository institution in the United States, and any company that owns or controls such a foreign bank, that has made an effective election under § 225.92 in the same manner and to the same extent as they apply to a financial holding company.

INTERPRETATIONS

§ 225.101 Bank holding company's subsidiary banks owning shares of nonbanking companies.

(a) The Board's opinion has been requested on the following related matters under the Bank Holding Company Act of 1956.

(b) The question is raised as to whether shares in a nonbanking company which were acquired by a banking subsidiary of the bank holding company many years ago when their acquisition was lawful and are now held as investments, and which do not include more than 5 percent of the outstanding voting securities of such nonbanking company and do not have a value greater than 5 percent of the value of the bank holding company's total assets, are exempted from the divestment requirements of the Act by the provisions of section 4(c)(5) of the Act.

(c) In the Board's opinion, this exemption is as applicable to such shares when held by a banking subsidiary of a bank holding company as when held directly by the bank holding company itself. While the exemption specifically refers only to shares held or acquired by the bank holding company, the prohibition of the Act against retention of

nonbanking interests applies to indirect as well as direct ownership of shares of a nonbanking company, and, in the absence of a clear mandate to the contrary, any exception to this prohibition should be given equal breadth with the prohibition. Any other interpretation would lead to unwarranted results.

(d) Although certain of the other exemptions in section 4(c) of the Act specifically refer to shares held or acquired by banking subsidiaries, an analysis of those exemptions suggests that such specific reference to banking subsidiaries was for the purpose of excluding nonbanking subsidiaries from such exemptions, rather than for the purpose of providing an inclusionary emphasis on banking subsidiaries.

(e) It should be noted that the Board's view as to this question should not be interpreted as meaning that each banking subsidiary could own up to 5 percent of the stock of the same nonbanking organization. In the Board's opinion the limitations set forth in section 4(c)(5) apply to the aggregate amount of stock held in a particular organization by the bank holding company itself and by all of its subsidiaries.

(f) Secondly, question is raised as to whether shares in a nonbanking company acquired in satisfaction of debts previously contracted (d.p.c.) by a banking subsidiary of the bank holding company may be retained if such shares meet the conditions contained in section 4(c)(5) as to value and amount, notwithstanding the requirement of section 4(c)(2) that shares acquired d.p.c. be disposed of within two years after the date of their acquisition or the date of the Act, whichever is later. In the Board's opinion, the 5 percent exemption provided by section 4(c)(5) covers any shares, including shares acquired d.p.c., that meet the conditions set forth in that exemption, and, consequently, d.p.c. shares held by a banking subsidiary of a bank holding company which meet such conditions are not subject to the two-year disposition requirement prescribed by section 4(c)(2), although any such shares would, of course, continue to be subject to such requirement for disposition as may be prescribed by provisions of any applicable banking laws or by the appropriate bank supervisory authorities.

(g) Finally, question is raised as to whether shares held by banking subsidiaries of the bank holding company in companies holding bank premises of such subsidiaries are exempted from the divestment requirements by section 4(c)(1) of the Act. It is the Board's view that section 4(c)(1), exempting shares owned or acquired by a bank holding company in any company engaged solely in holding or operating properties used wholly or substantially by any subsidiary bank, is to be read and interpreted, like section 4(c)(5), as applying to shares owned indirectly by a bank holding company through a banking subsidiary as well as to shares held directly by the bank holding company. A contrary interpretation would impair the right that member banks controlled by bank holding companies would otherwise have to invest, subject to the limitations of section 24A of the Federal Reserve Act, in stock of companies holding their bank premises; and such a result was not, in the Board's opinion, intended by the Bank Holding Company Act.

[21 FR 10472, Dec. 29, 1956. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.102 Bank holding company indirectly owning nonbanking company through subsidiaries.

(a) The Board of Governors has been requested for an opinion regarding the exemptions contained in section 4(c)(5) of the Bank Holding Company Act of 1956. It is stated that Y Company is an investment company which is not a bank holding company and which is not engaged in any business other than investing in securities, which securities do not include more than 5 per centum of the outstanding voting securities of any company and do not include any asset having a value greater than 5 per centum of the value of the total assets of X Corporation, a bank holding company. It is stated that direct ownership by X Corporation of voting shares of Y Company would be exempt by reason of section 4(c)(5) from the prohibition of section 4 of the Act against ownership by bank holding companies of nonbanking assets.

(b) It was asked whether it makes any difference that the shares of Y Company are not owned directly by X Corporation but instead are owned through Subsidiaries A and B. X Corporation owns all the voting shares of Subsidiary A, which owns one-half of the voting shares of Subsidiary B. Subsidiaries A and B each own one-third of the voting shares of Y Company.

(c) Section 4(c)(5) is divided into two parts. The first part exempts the ownership of securities of nonbanking companies when the securities do not include more than 5 percent of the voting securities of the nonbanking company and do not have a value greater than 5 percent of the value of the total assets of the bank holding company. The second part exempts the ownership of securities of an investment company which is not a bank holding company and is not engaged in any business other than investing in securities, provided the securities held by the investment company meet the 5 percent tests mentioned above.

(d) In § 225.101, the Board expressed the opinion that the first exemption in section 4(c)(5):

> * * * is as applicable to such shares when held by a banking subsidiary of a bank holding company as when held directly by the bank holding company itself. While the exemption specifically refers only to shares held or acquired by the bank holding company, the prohibition of the Act against retention of nonbanking interests applies to indirect as well as direct ownership of shares of a nonbanking company, and, in the absence of a clear mandate to the contrary, any exception to this prohibition should be given equal breadth with the prohibition. Any other interpretation would lead to unwarranted results.

(e) The Board is of the view that the principles stated in that opinion are also applicable to the second exemption in section 4(c)(5), and that they apply whether or not the subsidiary owning the shares is a banking subsidiary. Accordingly, on the basis of the facts presented, the Board is of the opinion that the second exemption in section 4(c)(5) applies to the indirect ownership by X Corporation of shares of Y Company through Subsidiaries A and B.

[22 FR 2533, Apr. 13, 1957. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.103 Bank holding company acquiring stock by dividends, stock splits or exercise of rights.

(a) The Board of Governors has been asked whether a bank holding company may receive bank stock dividends or participate in bank stock splits without the Board's prior approval, and whether such a company may exercise, without the Board's prior approval, rights to subscribe to new stock issued by banks in which the holding company already owns stock.

(b) Neither a stock dividend nor a stock split results in any change in a stockholder's proportional interest in the issuing company or any increase in the assets of that company. Such a transaction would have no effect upon the extent of a holding company's control of the bank involved; and none of the five factors required by the Bank Holding Company Act to be considered by the Board in approving a stock acquisition would seem to have any application. In view of the objectives and purposes of the act, the word ''acquire'' would not seem reasonably to include transactions of this kind.

(c) On the other hand, the exercise by a bank holding company of the right to subscribe to an issue of additional stock of a bank could result in an increase in the holding company's proportional interest in the bank. The holding company would voluntarily pay additional funds for the extra shares and would ''acquire'' the additional stock even under a narrow meaning of that term. Moreover, the exercise of such rights would cause the assets of the issuing company to be increased and in a sense, therefore, the ''size or extent'' of the bank holding company system would be expanded.

(d) In the circumstances, it is the Board's opinion that receipt of bank stock by means of a stock dividend or stock split, assuming no change in the class of stock, does not require the Board's prior approval under the act, but that purchase of bank stock by a bank holding company through the exercise of rights does require the Board's prior approval, unless one of the exceptions set forth in section 3(a) is applicable.

[22 FR 7461, Sept. 19, 1957. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.104 "Services" under section 4(c)(1) of Bank Holding Company Act.

(a) Section 4(c)(1) of the Bank Holding Company Act, among other things, exempts from the nonbanking divestment requirements of section 4(a) of the Act shares of a company engaged ''solely in the business of furnishing services to or performing services for'' its bank holding company or subsidiary banks thereof.

(b) The Board of Governors has had occasion to express opinions as to whether this section of law applies to the following two sets of facts:

(1) In the first case, Corporation X, a nonbanking subsidiary of a bank holding company (Holding Company A), was engaged in the business of purchasing installment paper suitable for investment by banking subsidiaries of Holding Company A. All installment paper purchased by Corporation X was sold by it to a bank which is a subsidiary of Holding Company A, without recourse, at a price equal to the cost of the installment paper to Corporation X, and with compensation to the latter based on the earnings from such paper remaining after certain reserves, expenses and charges. The subsidiary bank sold participations in such installment paper to the other affiliated banks of Holding Company A which desired to participate. Purchases by Corporation X consisted mainly of paper insured under Title I of the National Housing Act and, in addition, Corporation X purchased time payment contracts covering sales of appliances by dealers under contractual arrangements with utilities, as well as paper covering home improvements which was not insured. Pursuant to certain service agreements, Corporation X made all collections, enforced guaranties, filed claims under Title I insurance and performed other services for the affiliated banks. Also Corporation X rendered to banking subsidiaries of Holding Company A various accounting, statistical and advisory services such as payroll, life insurance and budget loan installment account.

(2) In the second case, Corporation Y, a nonbanking subsidiary of a bank holding company (Holding Company B, which was also a bank), solicited business on behalf of Holding Company B from dealers, throughout several adjoining or contiguous States, who made time sales and desired to convert their time sales paper into cash; but Corporation Y made no loans or purchases of sales contracts and did not discount or advance money for time sales obligations. Corporation Y investigated credit standings of purchasers obligated on time sale contracts to be acquired by Holding Company B, Corporation Y received from dealers the papers offered by them and inspected such papers to see that they were in order, and transmitted to Holding Company B for its determination to purchase, including, in some cases, issuance of drafts in favor of dealers in order to facilitate their prompt receipt of payment for installment paper purchased by Holding Company B. Corporation Y made collections of delinquent paper or delinquent installments, which sometimes involved repossession and resale of the automobile or other property which secured the paper. Also, upon request of purchasers obligated on paper held by Holding Company B, Corporation Y transmitted installment payments to Holding Company B. Holding Company B reimbursed Corporation Y for its actual costs and expenses in performing the services mentioned above, including the salaries and wages of all Corporation Y officers and employees.

(c) While the term ''services'' is sometimes used in a broad and general sense, the legislative history of the Bank Holding Company Act indicates that in section 4(c)(1) the word was meant to be somewhat more limited in its application. An early version of the bill specifically exempted companies engaged in serving the bank holding company and its subsidiary banks in ''auditing, appraising, investment counseling''. The statute as finally enacted does not expressly mention any specific type of servicing activity for exemption. In recommending the change, the Senate Banking and Currency Committee stated that the types of services contemplated are ''in the fields of advertising, public relations, developing new business, organizations,

operations, preparing tax returns, personnel, and many others'', which indicates that latitude should be given to the range of activities contemplated by this section beyond those specifically set forth in the early draft of the bill. (84th Cong., 2d Sess., Senate Report 1095, Part 2, p. 3.) It nevertheless seems evident that Congress intended such services to be types of activities generally comparable to those mentioned above from the early bill (''auditing, appraising, investment counseling'') and in the excerpt from the Committee Report on the later bill (''advertising, public relations, developing new business, organization, operations, preparing tax returns, personnel, and many others''). This legislative history and the context in which the term ''services'' is used in section 4(c)(1) seem to suggest that the term was in general intended to refer to servicing operations which a bank could carry on itself, but which the bank or its holding company chooses to have done through another organization. Moreover, the report of the Senate Banking and Currency Committee indicated that the types of servicing permitted under section 4(c)(1) are to be distinguished from activities of a ''financial, fiduciary, or insurance nature'', such as those which might be considered for possible exemption under section 4(c)(6) of the Act.

(d) With respect to the first set of facts, the Board expressed the opinion that certain of the activities of Corporation X, such as the accounting, statistical and advisory services referred to above, may be within the range of servicing activities contemplated by section 4(c)(1), but that this would not appear to be the case with the main activity of Corporation X, which was the purchase of installment paper and the resale of such paper at cost, without recourse, to banking subsidiaries of Holding Company A. This latter and basic activity of Corporation X appeared to involve essentially a financial relationship between it and the banking subsidiaries of Holding Company A and appeared beyond the category of servicing exemptions contemplated by section 4(c)(1) of the Act. Accordingly, it was the Board's view that Corporation X could not be regarded as qualifying under section 4 (c)(1) as a company engaged ''solely in the business of furnishing services to or performing services for'' Holding Company A or subsidiary banks thereof.

(e) With respect to the second set of facts, the Board expressed the opinion that some of the activities engaged in by Corporation Y were clearly within the range of servicing activities contemplated by section 4(c)(1). There was some question as to whether or not some of the other activities of Corporation Y mentioned above could meet the test, but on balance, it seemed that all such activities probably were activities in which Holding Company B, which as already indicated was a bank, could itself engage, at the present locations of Corporation Y, without being engaged in the operation of bank branches at those locations. In the circumstances, while the question was not free from doubt, the Board expressed the opinion that the activities of Corporation Y were those of a company engaged ''solely in the business of furnishing services to or performing services for'' Holding Company B within the meaning of section 4(c)(1) of the Act, and that, accordingly, the control by Holding Company B of shares in Corporation Y was exempted under that section.

[23 FR 2675, May 23, 1958. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.107 Acquisition of stock in small business investment company.

(a) A registered bank holding company requested an opinion by the Board of Governors with respect to whether that company and its banking subsidiaries may acquire stock in a small business investment company organized pursuant to the Small Business Investment Act of 1958.

(b) It is understood that the bank holding company and its subsidiary banks propose to organize and subscribe for stock in a small business investment company which would be chartered pursuant to the Small Business Investment Act of 1958 which provides for long-term credit and equity financing for small business concerns.

(c) Section 302(b) of the Small Business Investment Act authorizes national banks, as well as other member banks and nonmember insured banks to the extent permitted by applicable State law, to invest capital in small business investment companies not exceeding one percent of the capital and surplus of such banks. Section 4(c)(4) of the Bank Holding Company Act exempts from the prohibitions of section 4 of the Act ''shares which are of the kinds and amounts eligible for investment by National banking associations under the provisions of section 5136 of the Revised Statutes''. Section 5136 of the Revised Statutes (paragraph ''Seventh'') in turn provides, in part, as follows:

> Except as hereinafter provided or otherwise permitted by law nothing herein contained shall authorize the purchase by the association for its own account of any shares of stock of any corporation.

Since the shares of a small business investment company are of a kind and amount expressly made eligible for investment by a national bank under the Small Business Investment Act of 1958, it follows, therefore, that the ownership or control of such shares by a bank holding company would be exempt from the prohibitions of section 4 of the Bank Holding Company Act by virtue of the provisions of section 4(c)(4) of that Act. Accordingly, the ownership or control of such shares by the bank holding company would be exempt from the prohibitions of section 4 of the Bank Holding Company Act.

(d) An additional question is presented, however, as to whether section 6 of the Bank Holding Company Act prohibits banking subsidiaries of the bank holding company from purchasing stock in a small business investment company where the latter is a ''subsidiary'' under that Act.

(e) Section 6(a)(1) of the Act makes it unlawful for a bank to invest any of its funds in the capital stock of any other subsidiary of the bank holding company. However, section 6(a)(1) was, in effect, amended by section 302(b) of the Small Business Investment Act (15 U.S.C. 682) as amended by the Act of June 11, 1960 (Pub. L. 86–502) so as to nullify this prohibition when the ''subsidiary'' is a small business investment company.

(f) Accordingly, section 6 of the Bank Holding Company Act does not prohibit banking subsidiaries of the bank holding company from purchasing stock in a small business investment company organized pursuant to the Small Business Investment Act of 1958, where that company is or will be a subsidiary of the bank holding company.

[25 FR 7485, Aug. 9, 1960. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.109 "Services" under section 4(c)(1) of Bank Holding Company Act.

(a) The Board of Governors has been requested by a bank holding company for an interpretation under section 4(c)(1) of the Bank Holding Company Act which, among other things, exempts from the nonbanking divestment requirements of section 4(a) of the Act, shares of a company engaged ''solely in the business of furnishing services to or performing services for'' its bank holding company or subsidiary banks thereof.

(b) It is understood that a nonbanking subsidiary of the holding company engages in writing comprehensive automobile insurance (fire, theft, and collision) which is sold only to customers of a subsidiary bank of the holding company in connection with the bank's retail installment loans; that when payment is made on a loan secured by a lien on a motor vehicle, renewal policies are not issued by the insurance company; and that the insurance company receives the usual agency commissions on all comprehensive automobile insurance written for customers of the bank.

(c) It is also understood that the insurance company writes credit life insurance for the benefit of the bank and its installment-loan customers; that each insured debtor is covered for an amount equal to the unpaid balance of his note to the bank, not to exceed $5,000; that as the note is reduced by regular monthly payments, the amount of insurance is correspondingly reduced so that at all times the debtor is insured for the unpaid balance of his note; that each insurance contract provides for payment in full of the entire

loan balance upon the death or permanent disability of the insured borrower; and that this credit life insurance is written only at the request of, and solely for, the bank's borrowing customers. It is further understood that the insurance company engages in no other activity.

(d) As indicated in § 225.104 (23 FR 2675), the term ''services,'' while sometimes used in a broad and general sense, appears to be somewhat more limited in its application in section 4(c)(1) of the Bank Holding Company Act. Unlike an early version of the Senate bill (S. 2577, before amendment), the act as finally enacted does not expressly mention any type of servicing activity for exemption. The legislative history of the Act, however, as indicated in the relevant portion of the record of the Senate Banking and Currency Committee on amended S. 2577 (84th Cong., 2d Sess., Senate Report 1095, Part 2, p. 3) makes it evident that Congress had in mind the exemption of services comparable to the types of activities mentioned expressly in the early Senate bill (''auditing, appraising, investment counseling'') and in the Committee Report on the later bill (''advertising, public relations, developing new business, organization, operations, preparing tax returns, personnel, and many others''). Furthermore, this Committee Report expressly stated that the provision of section 4(c)(1) with respect to ''furnishing services to or performing services for'' was not intended to supplant the exemption contained under section 4 (c)(6) of the Act.

(e) The only activity of the insurance company (writing comprehensive automobile insurance and credit life insurance) appears to involve an insurance relationship between it and a banking subsidiary of the holding company which the legislative history clearly indicates does not come within the meaning of the phrase ''furnishing services to or performing services for'' a bank holding company or its banking subsidiaries.

(f) Accordingly, it is the Board's view that the insurance company could not be regarded as qualifying as a company engaged ''solely in the business of furnishing services to or performing services for'' the bank holding company or banks with respect to which the latter is a bank holding company.

[23 FR 9017, Nov. 20, 1958. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.111 Limit on investment by bank holding company system in stock of small business investment companies.

(a) Under the provisions of section 4(c)(5) of the Bank Holding Company Act, as amended (12 U.S.C. 1843), a bank holding company may acquire shares of nonbank companies ''which are of the kinds and amounts eligible for investment'' by national banks. Pursuant to section 302(b) of the Small Business Investment Act of 1958 (15 U.S.C. 682(b)), as amended by Title II of the Small Business Act Amendments of 1967 (Pub. L. 90–104, 81 Stat. 268, 270), a national bank may invest in stock of small business investment companies (SBICs) subject to certain restrictions.

(b) On the basis of the foregoing statutory provisions, it is the position of the Board that a bank holding company may acquire direct or indirect ownership or control of stock of an SBIC subject to the following limits:

(1) The total direct and indirect investments of a bank holding company in stock of SBICs may not exceed:

(i) With respect to all stock of SBICs owned or controlled directly or indirectly by a subsidiary bank, 5 percent of that bank's capital and surplus;

(ii) With respect to all stock of SBICs owned directly by a bank holding company that is a bank, 5 percent of that bank's capital and surplus; and

(iii) With respect to all stock of SBICs otherwise owned or controlled directly or indirectly by a bank holding company, 5 percent of its proportionate interest in the capital and surplus of each subsidiary bank (that is, the holding company's percentage of that bank's stock times that bank's capital and surplus) less that bank's investment in stock of SBICs; and

(2) A bank holding company may not acquire direct or indirect ownership or control of 50 percent or more of the shares of any class of equity securities of an SBIC that have actual or potential voting rights.

(c) A bank holding company or a bank subsidiary that acquired direct or indirect ownership or control of 50 percent or more of any such class of equity securities prior to January 9, 1968, is not required to divest to a level below 50 percent. A bank that acquired 50 percent or more prior to January 9, 1968, may become a subsidiary in a holding company system without any necessity for divesting to a level below 50 percent: *Provided*, That such action does not result in the bank holding company acquiring control of a percentage greater than that controlled by such bank.

(12 U.S.C. 248. Interprets 12 U.S.C. 1843, 15 U.S.C. 682)

[33 FR 6967, May 9, 1968. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.112 Indirect control of small business concern through convertible debentures held by small business investment company.

(a) A question has been raised concerning the applicability of provisions of the Bank Holding Company Act of 1956 to the acquisition by a bank holding company of stock of a small business investment company (''SBIC'') organized pursuant to the Small Business Investment Act of 1958 (''SBI Act'').

(b) As indicated in the interpretation of the Board (§ 225.107) published at 23 FR 7813, it is the Board's opinion that, since stock of an SBIC is eligible for purchase by national banks and since section 4(c)(4) of the Holding Company Act exempts stock eligible for investment by national banks from the prohibitions of section 4 of that Act, a bank holding company may lawfully acquire stock in such an SBIC.

(c) However, section 304 of the SBI Act provides that debentures of a small business concern purchased by a small business investment company may be converted at the option of such company into stock of the small business concern. The question therefore arises as to whether, in the event of such conversion, the parent bank holding company would be regarded as having acquired ''direct or indirect ownership or control'' of stock of the small business concern in violation of section 4(a) of the Holding Company Act.

(d) The Small Business Investment Act clearly contemplates that one of the primary purposes of that Act was to enable SBICs to provide needed equity capital to small business concerns through the purchase of debentures convertible into stock. Thus, to the extent that a stockholder in an SBIC might acquire indirect control of stock of a small business concern, such control appears to be a natural and contemplated incident of ownership of stock of the SBIC. The Office of the Comptroller of the Currency has informally indicated concurrence with this interpretation insofar as it affects investments by national banks in stock of an SBIC.

(e) Since the exception as to stock eligible for investment by national banks contained in section 4(c)(4) of the Holding Company Act was apparently intended to permit a bank holding company to acquire any stock that would be eligible for purchase by a national bank, it is the Board's view that section 4(a)(1) of the Act does not prohibit a bank holding company from acquiring stock of an SBIC, even though ownership of such stock may result in the acquisition of indirect ownership or control of stock of a small business concern which would not itself be eligible for purchase directly by a national bank or a bank holding company.

[24 FR 1584, Mar. 4, 1959. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.113 Services under section 4(a) of Bank Holding Company Act.

(a) The Board of Governors has been requested for an opinion as to whether the performance of certain functions by a bank holding company for four banks of which it owns less than 25 percent of the voting shares is in violation of section 4(a) of the Bank Holding Company Act.

(b) It is claimed that the holding company is engaged in ''managing'' four nonsubsidiary banks, for which services it receives ''management fees.'' Specifically, the company engages in the following activities for the four nonsubsidiary banks: (1) Establishment and supervision of loaning policies; (2) direction of the purchase and sale of investment securities; (3)

selection and training of officer personnel; (4) establishment and enforcement of operating policies; and (5) general supervision over all policies and practices.

(c) The question raised is whether these activities are prohibited by section 4(a)(2) of the Bank Holding Company Act, which permits a bank holding company to engage in only three categories of business: (1) Banking; (2) managing or controlling banks; and (3) furnishing services to or performing services for any bank of which the holding company owns or controls 25 percent or more of the voting shares.

(d) Clearly, the activities of the company with respect to the four nonsubsidiary banks do not constitute ''banking.'' With respect to the business of ''managing or controlling'' banks, it is the Board's view that such business, within the purview of section 4(a)(2), is essentially the exercise of a broad governing influence of the sort usually exercised by bank stockholders, as distinguished from direct or active participation in the establishment or carrying out of particular policies or operations. The latter kinds of activities fall within the third category of businesses in which a bank holding company is permitted to engage. In the Board's view, the activities enumerated above fall in substantial part within that third category.

(e) Section 4(a)(2), like all other sections of the Holding Company Act, must be interpreted in the light of all of its provisions, as well as in the light of other sections of the Act. The expression ''managing * * * banks,'' if it could be taken by itself, might appear to include activities of the sort enumerated. However, such an interpretation of those words would virtually nullify the last portion of section 4(a)(2), which permits a holding company to furnish services to or perform services for ''any bank of which it owns or controls 25 per centum or more of the voting shares.''

(f) Since Congress explicitly authorized the performance of services for banks that are at least 25 percent owned by a holding company, it obviously intended that the holding company should not perform services for banks in which it owns less than 25 percent of the voting shares. However, if the second category—''managing or controlling banks''—were interpreted to permit the holding company to perform services for any bank, including a bank in which it held less than 25 percent of the stock (or no stock whatsoever), the last clause of section 4(a)(2) would be meaningless.

(g) It is principally for this reason—that is, to give effective meaning to the final clause of section 4(a)(2)—that the Board interprets ''managing or controlling banks'' in that provision as referring to the exercise of a stockholder's management or control of banks, rather than direct and active participation in their operations. To repeat, such active participation in operations falls within the third category (''furnishing services to or performing services for any bank'') and consequently may be engaged in only with respect to banks in which the holding company ''owns or controls 25 per centum or more of the voting shares.''

(h) Accordingly, it is the Board's conclusion that, in performing the services enumerated, the bank holding company is ''furnishing services to or performing services for'' the four banks referred to. Under the Act such furnishing or performing of services is permissible only if the holding company owns or controls 25 percent of the voting shares of each bank receiving such services, and, since the company owns less than 25 percent of the voting shares of these banks, it follows that these activities are prohibited by section 4(a)(2).

(i) While this conclusion is required, in the Board's opinion, by the language of the statute, it may be noted further that any other conclusion would make it possible for bank holding company or any other corporation, through arrangements for the ''managing'' of banks in the manner here involved, to acquire effective control of banks without acquiring bank stocks and thus to evade the underlying objectives of section 3 of the Act.

[25 FR 281, Jan. 14, 1960. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.115 Applicability of Bank Service Corporation Act in certain bank holding company situations.

(a) Questions have been presented to the Board of Governors regarding the applicability of the recently enacted Bank Service Corporation Act (Pub. L. 87–856, approved October 23, 1962) in cases involving service corporations that are subsidiaries of bank holding companies under the Bank Holding Company Act of 1956. In addition to being charged with the administration of the latter Act, the Board is named in the Bank Service Corporation Act as the Federal supervisory agency with respect to the performance of bank services for State member banks.

(b) *Holding company-owned corporation serving only subsidiary banks.* (1) One question is whether the Bank Service Corporation Act is applicable in the case of a corporation, wholly owned by a bank holding company, which is engaged in performing ''bank services'', as defined in section 1(b) of the Act, exclusively for subsidiary banks of the holding company.

(2) Except as noted below with respect to section 5 thereof, the Bank Service Corporation Act is not applicable in this case. This is true because none of the stock of the corporation performing the services is owned by any bank and the corporation, therefore, is not a ''bank service corporation'' as defined in section 1(c) of the Act. A corporation cannot meet that definition unless part of its stock is owned by two or more banks. The situation clearly is unaffected by section 2(b) of the Act which permits a corporation that fell within the definition initially to continue to function as a bank service corporation although subsequently only one of the banks remains as a stockholder in the corporation.

(3) However, although it is not a bank service corporation, the corporation in question and each of the banks for which it performs bank services are subject to section 5 of the Bank Service Corporation Act. That section, which requires the furnishing of certain assurances to the appropriate Federal supervisory agency in connection with the performance of bank services for a bank, is applicable whether such services are performed by a bank service corporation or by others.

(4) Section 4(a)(1) of the Bank Holding Company Act prohibits the acquisition by a bank holding company of ''direct or indirect ownership or control'' of shares of a nonbanking company, subject to certain exceptions. Section 4(c)(1) of the Act exempts from section 4(a)(1) shares of a company engaged ''solely in the business of furnishing services to or performing services for'' its bank holding company or subsidiary banks thereof. Assuming that the bank services performed by the corporation in question are ''services'' of the kinds contemplated by section 4(c)(1) of the Bank Holding Company Act (as would be true, for example, of the electronic data processing of deposit accounts), the holding company's ownership of the corporation's shares in the situation described above clearly is permissible under that section of the Act.

(c) *Bank service corporation owned by holding company subsidiaries and serving also other banks.* (1) The other question concerns the applicability of the Bank Service Corporation Act and the Bank Holding Company Act in the case of a corporation, all the stock of which is owned either by a bank holding company and its subsidiary banks together or by the subsidiary banks alone, which is engaged in performing ''bank services'', as defined in section 1(b) of the Bank Service Corporation Act, for the subsidiary banks and for other banks, as well.

(2) In contrast to the situation under paragraph (b) of this section, the corporation in this case is a ''bank service corporation'' within the meaning of section 1(c) of the Bank Service Corporation Act because of the ownership by each of the subsidiary banks of a part of the corporation's stock. This stock ownership is one of the important facts differentiating this case from the first one. Being a bank service corporation, the corporation in question is subject to section 3 of the Act concerning applications to bank service corporations by competitive banks for bank services, and to section 4 forbidding a bank service corporation from engaging in any activity other than the performance of bank services

for banks. Section 5, mentioned previously and relating to ''assurances'', also is applicable in this case.

(3) The other important difference between this case and the situation in paragraph (b) of this section is that here the bank service corporation performs services for nonsubsidiary banks, as well as for subsidiary banks. This is permissible because section 2(a) of the Bank Service Corporation Act, which authorizes any two or more banks to invest limited amounts in a bank service corporation, removes all limitations and prohibitions of Federal law exclusively relating to banks that otherwise would prevent any such investment. From the legislative history of section 2(a), it is clear that section 6 of the Bank Holding Company Act is among the limitations and prohibitions so removed. But for such removal, section 6(a)(1) of that Act would make it unlawful for any of the subsidiary banks of the bank holding company in question to own stock in the bank service corporation subsidiary of the holding company, as the exemption in section 6(b)(1) would not apply because of the servicing by the bank service corporation of nonsubsidiary banks.

(4) Because the bank service corporation referred to in the question is serving banks other than the subsidiary banks, the bank holding company is not exempt under section 4(c)(1) of the Bank Holding Company Act from the prohibition of acquisition of nonbanking interests in section 4(a)(1) of that Act. The bank holding company, however, is entitled to the benefit of the exemption in section 4(c)(4) of the Act. That section exempts from section 4(a) ''shares which are of the kinds and amounts eligible for investment by National banking associations under the provisions of section 5136 of the Revised Statutes''. Section 5136 provides, in part, that: ''Except as hereinafter provided or otherwise permitted by law, nothing herein contained shall authorize the purchase by the association for its own account of any shares of stock of any corporation.'' As the provisions of section 2(a) of the Bank Service Corporation Act and its legislative history make it clear that shares of a bank service corporation are of a kind eligible for investment by national banks under section 5136, it follows that the direct or indirect ownership on control of such shares by a bank holding company are permissible within the amount limitation discussed in paragraph (d) of this section.

(d) *Limit on investment by bank holding company system in stock of bank service corporation.* (1) In the situation presented by paragraph (c) the bank holding company clearly owns or controls, directly or indirectly, all of the stock of the bank service corporation. The remaining question, therefore, is whether the total direct and indirect investment of the bank holding company in the bank service corporation exceeds the amount permissible under the Bank Holding Company Act.

(2) The effect of sections 4(a)(1) and 4(c)(4) of the Bank Holding Company Act is to limit the amount of shares of a bank service corporation that a bank holding company may own or control, directly or indirectly, to the amount eligible for investment by a national bank, as previously indicated. Under section 2(a) of the Bank Service Corporation Act, the amount of shares of a bank service corporation eligible for investment by a national bank may not exceed ''10 per centum [of the bank's] * * * paid-in and unimpaired capital and unimpaired surplus''.

(3) The Board's view is that this aspect of the matter should be determined in accordance with the principles set forth in § 225.111, as revised (27 FR 12671), involving the application of sections 4(a)(1) and 4(c)(4) of the Bank Holding Company Act in the light of section 302(b) of the Small Business Investment Act limiting the amount eligible for investment by a national bank in the shares of a small business investment company to two percent of the bank's ''capital and surplus''.

(4) Except for the differences in the percentage figures, the investment limitation in section 302(b) of the Small Business Investment Act is essentially the same as the investment limitation in section 2(a) of the Bank Service Corporation Act since, as an accounting matter and for the purposes under consideration, ''capital and surplus'' may be regarded as equivalent in meaning to ''paid-in and unimpaired capital and

unimpaired surplus.'' Accordingly, the maximum permissible investment by a bank holding company system in the stock of a bank service corporation should be determined in accordance with the formula prescribed in § 222.111.

[27 FR 12918, Dec. 29, 1962. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.118 Computer services for customers of subsidiary banks.

(a) The question has been presented to the Board of Governors whether a wholly-owned nonbanking subsidiary (''service company'') of a bank holding company, which is now exempt from the prohibitions of section 4 of the Bank Holding Company Act of 1956 (''the Act'') because its sole business is the providing of services for the holding company and the latter's subsidiary banks, would lose its exempt status if it should provide data processing services for customers of the subsidiary banks.

(b) The Board understood from the facts presented that the service company owns a computer which it utilizes to furnish data processing services for the subsidiary banks of its parent holding company. Customers of these banks have requested that the banks provide for them computerized billing, accounting, and financial records maintenance services. The banks wish to utilize the computer services of the service company in providing these and other services of a similar nature. It is proposed that, in each instance where a subsidiary bank undertakes to provide such services, the bank will enter into a contract directly with the customer and then arrange to have the service company perform the services for it, the bank. In no case will the service company provide services for anyone other than its affiliated banks. Moreover, it will not hold itself out as, nor will its parent corporation or affiliated banks represent it to be, authorized or willing to provide services for others.

(c) Section 4(c)(1) of the Act permits a holding company to own shares in ''any company engaged solely * * * in the business of furnishing services to or performing services for such holding company and banks with respect to which it is a bank holding company * * *.'' The Board has ruled heretofore that the term ''services'' as used in section 4(c)(1) is to be read as relating to those services (excluding ''closely related'' activities of ''a financial, fiduciary, or insurance nature'' within the meaning of section 4(c)(6)) which a bank itself can provide for its customers (§ 225.104). A determination as to whether a particular service may legitimately be rendered or performed by a bank for its customers must be made in the light of applicable Federal or State statutory or regulatory provisions. In the case of a State-chartered bank, the laws of the State in which the bank operates, together with any interpretations thereunder rendered by appropriate bank authorities, would govern the right of the bank to provide a particular service. In the case of a national bank, a similar determination would require reference to provisions of Federal law relating to the establishment and operation of national banks, as well as to pertinent rulings or interpretations promulgated thereunder.

(d) Accordingly, on the assumption that all of the services to be performed are of the kinds that the holding company's subsidiary banks may render for their customers under applicable Federal or State law, the Board concluded that the rendition of such services by the service company for its affiliated banks would not adversely affect its exempt status under section 4(c)(1) of the Act.

(e) In arriving at the above conclusion, the Board emphasized that its views were premised explicitly upon the facts presented to it, and particularly its understanding that banks are permitted, under applicable Federal or State law to provide the proposed computer services. The Board emphasized also that in respect to the service company's operations, there continues in effect the requirement under section 4(c)(1) that the service company engage solely in the business of furnishing services to or performing services for the bank holding company and its subsidiary banks. The Board added that any substantial change in the facts that had been presented might require re-examination of the service company's status under section 4(c)(1).

[29 FR 12361, Aug. 28, 1964. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.121 Acquisition of Edge corporation affiliate by State member banks of registered bank holding company.

(a) The Board has been asked whether it is permissible for the commercial banking affiliates of a bank holding company registered under the Bank Holding Company Act of 1956, as amended, to acquire and hold the shares of the holding company's Edge corporation subsidiary organized under section 25(a) of the Federal Reserve Act.

(b) Section 9 of the Bank Holding Company Act amendments of 1966 (Pub. L. 89–485, approved July 1, 1966) repealed section 6 of the Bank Holding Company Act of 1956. That rendered obsolete the Board's interpretation of section 6 that was published in the March 1966 Federal Reserve Bulletin, page 339 (§ 225.120). Thus, so far as Federal Banking law applicable to State member banks is concerned, the answer to the foregoing question depends on the provisions of section 23A of the Federal Reserve Act, as amended by the 1966 amendments to the Bank Holding Company Act. By its specific terms, the provisions of section 23A do not apply to an affiliate organized under section 25(a) of the Federal Reserve Act.

(c) Accordingly, the Board concludes that, except for such restrictions as may exist under applicable State law, it would be legally permissible by virtue of paragraph 20 of section 9 of the Federal Reserve Act for any or all of the State member banks that are affiliates of a registered bank holding company to acquire and hold shares of the Edge corporation subsidiary of the bank holding company within the amount limitation in the last sentence of paragraph 12 of section 25(a) of the Federal Reserve Act.

(12 U.S.C. 24, 248, 335, 371c, 611, 618)

[31 FR 10263, July 29, 1966. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.122 Bank holding company ownership of mortgage companies.

(a) The Board of Governors recently considered whether a bank holding may acquire, either directly or through a subsidiary, the stock of a so-called ''mortgage company'' that would be operated on the following basis: The company would solicit mortgage loans on behalf of a bank in the holding company system, assemble credit information, make property inspections and appraisals, and secure title information. The company would also participate in the preparation of applications for mortgage loans, which it would submit, together with recommendations with respect to action thereon, to the bank, which alone would decide whether to make any or all of the loans requested. The company would in addition solicit investors to purchase mortgage loans from the bank and would seek to have such investors contract with the bank for the servicing of such loans.

(b) Under section 4 of the Bank Holding Company Act (12 U.S.C. 1843), a bank holding company is generally prohibited from acquiring ''direct or indirect ownership'' of stock of nonbanking corporations. The two exceptions principally involved in the question presented are with respect to (1) stock that is eligible for investment by a national bank (section 4(c)(5) of the Act) and (2) shares of a company ''furnishing services to or performing services for such bank holding company or its banking subsidiaries'' (section 4(c)(1)(C) of the Act).

(c) The Board has previously indicated its view that a national bank is forbidden by the so-called ''stock-purchase prohibition'' of paragraph ''Seventh'' of section 5136 of the Revised Statutes (12 U.S.C. 24) to purchase ''for its own account * * * any shares of stock of any corporation'' except (1) to the extent permitted by specific provisions of Federal law or (2) as comprised within the concept of ''such incidental powers as shall be necessary to carry on the business of banking'' referred to in the first sentence of said paragraph ''Seventh''. There is no specific statutory provision authorizing a national bank to purchase stock in a mortgage company, and in the Board's view such purchase may not properly be regarded as authorized under the ''incidental powers'' clause. (See 1966 Federal Reserve Bulletin 1151; 12 CFR 208.119.) Accordingly, a bank holding company may not acquire stock in a mortgage

company on the basis of the section 4(c)(5) exemption.

(d) However, the Board does not believe that such conclusion prejudices consideration of the question whether such a company is within the section 4(c)(1)(C) ''servicing exemption''. The basic purpose of section 4 of the Act is to confine a bank holding company's activities to the management and control of banks. In determining whether an activity in which a bank could itself engage is within the servicing exemption, the question is simply whether such activity may appropriately be considered as ''furnishing services to or performing services for'' a bank.

(e) As indicated in the Board's interpretation published in the 1958 Federal Reserve Bulletin at page 431 (12 CFR 225.104), the legislative history of the servicing exemption indicates that it includes the following activities: ''auditing, appraising, investment counseling'' and ''advertising, public relations, developing new business, organization, operations, preparing tax returns, and personnel''. The legislative history further indicates that some other activities also are within the scope of the exemption. However, the types of servicing permitted under such exemption must be distinguished from activities of a ''financial fiduciary, or insurance nature'', such as those that might be considered for possible exemption under section 4(c)(8) of the Act.

(f) In considering the interrelation of these exemptions in the light of the purpose of the prohibition against bank holding company interests in nonbanking organizations, the Board has concluded that the appropriate test for determining whether a mortgage company may be considered as within the servicing exemption is whether the company will perform as principal any banking activities—such as receiving deposits, paying checks, extending credit, conducting a trust department, and the like. In other words, if the mortgage company is to act merely as an adjunct to a bank for the purpose of facilitating the banks operations, the company may appropriately be considered as within the scope of the servicing exemption.[1]

(g) On this basis the Board concluded that, insofar as the Bank Holding Company Act is concerned, a bank holding company may acquire, either directly or through a subsidiary, the stock of a mortgage company whose functions are as described in the question presented. On the other hand, in the Board's view, a bank holding company may not acquire, on the basis of the servicing exemption, a mortgage company whose functions include such activities as extending credit for its own account, arranging interim financing, entering into mortgage service contracts on a fee basis, or otherwise performing functions other than solely on behalf of a bank.

(12 U.S.C. 248)

[32 FR 15004, Oct. 3, 1967, as amended at 35 FR 19662, Dec. 29, 1970. Redesignated at 36 FR 21666, Nov. 12, 1971]

§ 225.123 Activities closely related to banking.

(a) Effective June 15, 1971, the Board of Governors has amended § 225.4(a) of Regulation Y to implement its regulatory authority under section 4(c)(8) of the Bank Holding Company Act. In some respects activities determined by the Board to be closely related to banking are described in general terms that will require interpretation from time to time. The Board's views on some questions that have arisen are set forth below.

(b) Section 225.4(a) states that a company whose ownership by a bank holding company is authorized on the basis of that section may engage solely in specified activities. That limitation refers only to activities the authority for which depends on section 4(c)(8) of the Act. It does not prevent a holding company from establishing one subsidiary

[1] Insofar as the 1958 interpretation referred to above suggested that the branch banking laws are an appropriate general test for determining the scope of the servicing exemption, such interpretation is hereby modified. In view of the different purposes to be served by the branch banking laws and by section 4 of the Bank Holding Company Act, the Board has concluded that basing determinations under the latter solely on the basis of determinations under the former is inappropriate.

to engage, for example, in activities specified in § 225.4(a) and also in activities that fall within the scope of section 4(c)(1)(C) of the Act—the ''servicing'' exemption.

(c) The amendments to § 225.4(a) do not apply to restrict the activities of a company previously approved by the Board on the basis of section 4(c)(8) of the Act. Activities of a company authorized on the basis of section 4(c)(8) either before the 1970 Amendments or pursuant to the amended § 225.4(a) may be shifted in a corporate reorganization to another company within the holding company system without complying with the procedures of § 225.4(b), as long as all the activities of such company are permissible under one of the exemptions in section 4 of the Act.

(d) Under the procedures in § 225.4(a)(c), a holding company that wishes to change the location at which it engages in activities authorized pursuant to § 225.4(a) must publish notice in a newspaper of general circulation in the community to be served. The Board does not regard minor changes in location as within the coverage of that requirement. A move from one site to another within a 1-mile radius would constitute such a minor change if the new site is in the same State.

(e) Data processing. In providing packaged data processing and transmission services for banking, financial and economic data for installation on the premises of the customer, as authorized by § 225.4(a)(8)(ii), a bank holding company should limit its activities to providing facilities that perform banking functions, such as check collection, or other similar functions for customers that are depository or other similar institutions, such as mortgage companies. In addition, the Board regards the following as incidental activities necessary to carry on the permissible activities in this area:

(1) Providing excess capacity, not limited to the processing or transmission of banking, financial or economic data on data processing or transmission equipment or facilities used in connection with permissible data processing and data transmission activities, where:

(A) Equipment is not purchased solely for the purpose of creating excess capacity;

(B) Hardware is not offered in connection therewith; and

(C) Facilities for the use of the excess capacity do not include the provision of any software, other than systems software (including language), network communications support, and the operating personnel and documentation necessary for the maintenance and use of these facilities.

(2) Providing by-products of permissible data processing and data transmission activities, where not designed, or appreciably enhanced, for the purpose of marketability.

(3) Furnishing any data processing service upon request of a customer if such data processing service is not otherwise reasonably available in the relevant market area; and

In order to eliminate or reduce to an insignificant degree any possibility of unfair competition where services, facilities, by-products or excess capacity are provided by a bank holding company's nonbank subsidiary or related entity, the entity providing the services, facilities, by-products and/or excess capacity should have separate books and financial statements, and should provide these books and statements to any new or renewal customer requesting financial data. Consolidated or other financial statements of the bank holding company should not be provided unless specifically requested by the customer.

(Interprets and applies 12 U.S.C. 1843 (c)(8))

[36 FR 10778, June 3, 1971, as amended at 36 FR 11806, June 19, 1971. Redesignated at 36 FR 21666, Nov. 12, 1971 and amended at 40 FR 13477, Mar. 27, 1975; 47 FR 37372, Aug. 26, 1982; 52 FR 45161, Nov. 25, 1987]

§ 225.124 Foreign bank holding companies.

(a) Effective December 1, 1971, the Board of Governors has added a new § 225.4(g) to Regulation Y implementing its authority under section 4(c)(9) of the Bank Holding Company Act. The Board's views on some questions that have arisen in connection with the meaning of terms used in § 225.4(g) are set forth in paragraphs (b) through (g) of this section.

(b) The term ''activities'' refers to nonbanking activities and does not include the banking activities that foreign banks conduct in the United States through branches or agencies licensed under the banking laws of any State of the United States or the District of Columbia.

(c) A company (including a bank holding company) will not be deemed to be engaged in ''activities'' in the United States merely because it exports (or imports) products to (or from) the United States, or furnishes services or finances goods or services in the United States, from locations outside the United States. A company is engaged in ''activities'' in the United States if it owns, leases, maintains, operates, or controls any of the following types of facilities in the United States:

(1) A factory,

(2) A wholesale distributor or purchasing agency,

(3) A distribution center,

(4) A retail sales or service outlet,

(5) A network of franchised dealers,

(6) A financing agency, or

(7) Similar facility for the manufacture, distribution, purchasing, furnishing, or financing of goods or services locally in the United States.

A company will not be considered to be engaged in ''activities'' in the United States if its products are sold to independent importers, or are distributed through independent warehouses, that are not controlled or franchised by it.

(d) In the Board's opinion, section 4(a)(1) of the Bank Holding Company Act applies to ownership or control of shares of stock as an investment and does not apply to ownership or control of shares of stock in the capacity of an underwriter or dealer in securities. Underwriting or dealing in shares of stock are nonbanking activities prohibited to bank holding companies by section 4(a)(2) of the Act, unless otherwise exempted. Under §225.4(g) of Regulation Y, foreign bank holding companies are exempt from the prohibitions of section 4 of the Act with respect to their activities outside the United States; thus foreign bank holding companies may underwrite or deal in shares of stock (including shares of United States issuers) to be distributed outside the United States, provided that shares so acquired are disposed of within a reasonable time.

(e) A foreign bank holding company does not ''indirectly'' own voting shares by reason of the ownership or control of such voting shares by any company in which it has a noncontrolling interest. A foreign bank holding company may, however, ''indirectly'' control such voting shares if its noncontrolling interest in such company is accompanied by other arrangements that, in the Board's judgment, result in control of such shares by the bank holding company. The Board has made one exception to this general approach. A foreign bank holding company will be considered to indirectly own or control voting shares of a bank if that bank holding company acquires more than 5 percent of any class of voting shares of another bank holding company. A bank holding company may make such an acquisition only with prior approval of the Board.

(f) A company is ''indirectly'' engaged in activities in the United States if any of its subsidiaries (whether or not incorporated under the laws of this country) is engaged in such activities. A company is not ''indirectly'' engaged in activities in the United States by reason of a noncontrolling interest in a company engaged in such activities.

(g) Under the foregoing rules, a foreign bank holding company may have a noncontrolling interest in a foreign company that has a U.S. subsidiary (but is not engaged in the securities business in the United States) if more than half of the foreign company's consolidated assets and revenues are located and derived outside the United States. For the purpose of such determination, the assets and revenues of the United States subsidiary would be counted among the consolidated assets and revenues of the foreign company to the extent required or permitted by generally accepted accounting principles in the United States. The foreign bank holding company would not, however, be permitted to ''indirectly'' control voting shares of the said U.S. subsidiary, as might be the case if there are other arrangements accompanying its noncontrolling interest in the foreign parent company that, in the Board's judgment, result in control of

such shares by the bank holding company.

(Interprets and applies 12 U.S.C. 1843 (a) (1), (2), and (c)(9))

[36 FR 21808, Nov. 16, 1971]

§ 225.125 Investment adviser activities.

(a) Effective February 1, 1972, the Board of Governors amended § 225.4(a) of Regulation Y to add ''serving as investment adviser, as defined in section 2(a)(20) of the Investment Company Act of 1940, to an investment company registered under that Act'' to the list of activities it has determined to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. During the course of the Board's consideration of this amendment several questions arose as to the scope of such activity, particularly in view of certain restrictions imposed by sections 16, 20, 21, and 32 of the Banking Act of 1933 (12 U.S.C. 24, 377, 378, 78) (sometimes referred to hereinafter as the ''Glass-Steagall Act provisions'') and the U.S. Supreme Court's decision in Investment Company Institute v. Camp, 401 U.S. 617 (1971). The Board's views with respect to some of these questions are set forth below.

(b) It is clear from the legislative history of the Bank Holding Company Act Amendments of 1970 (84 Stat. 1760) that the Glass-Steagall Act provisions were not intended to be affected thereby. Accordingly, the Board regards the Glass-Steagall Act provisions and the Board's prior interpretations thereof as applicable to a holding company's activities as an investment adviser. Consistently with the spirit and purpose of the Glass-Steagall Act, this interpretation applies to all bank holding companies registered under the Bank Holding Company Act irrespective of whether they have subsidiaries that are member banks.

(c) Under § 225.4(a)(5), as amended, bank holding companies (which term, as used herein, includes both their bank and nonbank subsidiaries) may, in accordance with the provisions of § 225.4 (b), act as investment advisers to various types of investment companies, such as ''open-end'' investment companies (commonly referred to as ''mutual funds'') and ''closed-end'' investment companies. Briefly, a mutual fund is an investment company which, typically, is continuously engaged in the issuance of its shares and stands ready at any time to redeem the securities as to which it is the issuer; a closed-end investment company typically does not issue shares after its initial organization except at infrequent intervals and does not stand ready to redeem its shares.

(d) The Board intends that a bank holding company may exercise all functions that are permitted to be exercised by an ''investment adviser'' under the Investment Company Act of 1940, except to the extent limited by the Glass-Steagall Act provisions, as described, in part, hereinafter.

(e) The Board recognizes that presently most mutual funds are organized, sponsored and managed by investment advisers with which they are affiliated and that their securities are distributed to the public by such affiliated investment advisers, or subsidiaries or affiliates thereof. However, the Board believes that (1) The Glass-Steagall Act provisions do not permit a bank holding company to perform all such functions, and (2) It is not necessary for a bank holding company to perform all such functions in order to engage effectively in the described activity.

(f) In the Board's opinion, the Glass-Steagall Act provisions, as interpreted by the U.S. Supreme Court, forbid a bank holding company to sponsor, organize, or control a mutual fund. However, the Board does not believe that such restrictions apply to closed-end investment companies as long as such companies are not primarily or frequently engaged in the issuance, sale, and distribution of securities. A bank holding company should not act as investment adviser to an investment company that has a name similar to the name of the holding company or any of its subsidiary banks, unless the prospectus of the investment company contains the disclosures required in paragraph (h) of this section. In no case should a bank holding company act as investment adviser to an investment company that has either the same

name as the name of the holding company or any of its subsidiary banks, or a name that contains the word ''bank.''

(g) In view of the potential conflicts of interests that may exist, a bank holding company and its bank and nonbank subsidiaries should not purchase in their sole discretion, in a fiduciary capacity (including as managing agent), securities of any investment company for which the bank holding company acts as investment adviser unless, the purchase is specifically authorized by the terms of the instrument creating the fiduciary relationship, by court order, or by the law of the jurisdiction under which the trust is administered.

(h) Under section 20 of the Glass-Steagall Act, a member bank is prohibited from being affiliated with a company that directly, or through a subsidiary, engages principally in the issue, flotation, underwriting, public sale, or distribution of securities. A bank holding company or its nonbank subsidiary may not engage, directly or indirectly, in the underwriting, public sale or distribution of securities of any investment company for which the holding company or any nonbank subsidiary provides investment advice except in compliance with the terms of section 20, and only after obtaining the Board's approval under section 4 of the Bank Holding Company Act and subject to the limitations and disclosures required by the Board in those cases. The Board has determined, however, that the conduct of securities brokerage activities by a bank holding company or its nonbank subsidiaries, when conducted individually or in combination with investment advisory activities, is not deemed to be the underwriting, public sale, or distribution of securities prohibited by the Glass-Steagall Act, and the U.S. Supreme Court has upheld that determination. *See Securities Industry Ass'n* v. *Board of Governors,* 468 U.S. 207 (1984); *see also Securities Industry Ass'n* v. *Board of Governors,* 821 F.2d 810 (D.C. Cir. 1987), *cert. denied,* 484 U.S. 1005 (1988). Accordingly, the Board believes that a bank holding company or any of its nonbank subsidiaries that has been authorized by the Board under the Bank Holding Company Act to conduct securities brokerage activities (either separately or in combination with investment advisory activities) may act as agent, upon the order and for the account of customers of the holding company or its nonbank subsidiary, to purchase or sell shares of an investment company for which the bank holding company or any of its subsidiaries acts as an investment adviser. In addition, a bank holding company or any of its nonbank subsidiaries that has been authorized by the Board under the Bank Holding Company Act to provide investment advice to third parties generally (either separately or in combination with securities brokerage services) may provide investment advice to customers with respect to the purchase or sale of shares of an investment company for which the holding company or any of its subsidiaries acts as an investment adviser. In the event that a bank holding company or any of its nonbank subsidiaries provides brokerage or investment advisory services (either separately or in combination) to customers in the situations described above, at the time the service is provided the bank holding company should instruct its officers and employees to caution customers to read the prospectus of the investment company before investing and must advise customers in writing that the investment company's shares are not insured by the Federal Deposit Insurance Corporation, and are not deposits, obligations of, or endorsed or guaranteed in any way by, any bank, unless that happens to be the case. The holding company or nonbank subsidiary must also disclose in writing to the customer the role of the company or affiliate as adviser to the investment company. These disclosures may be made orally so long as written disclosure is provided to the customer immediately thereafter. To the extent that a bank owned by a bank holding company engages in providing advisory or brokerage services to bank customers in connection with an investment company advised by the bank holding company or a nonbank affiliate, but is not required by the bank's primary regulator to make disclosures comparable to the disclosures required to be made by bank holding companies providing such services, the bank holding company should require

its subsidiary bank to make the disclosures required in this paragraph to be made by a bank holding company that provides such advisory or brokerage services.

(i) Acting in such capacities as registrar, transfer agent, or custodian for an investment company is not a selling activity and is permitted under § 225.4(a)(4) of Regulation Y. However, in view of potential conflicts of interests, a bank holding company which acts both as custodian and investment adviser for an investment company should exercise care to maintain at a minimal level demand deposit accounts of the investment company which are placed with a bank affiliate and should not invest cash funds of the investment company in time deposit accounts (including certificates of deposit) of any bank affiliate.

[37 FR 1464, Jan. 29, 1972, as amended by Reg. Y, 57 FR 30391, July 9, 1992; 61 FR 45875, Aug. 30, 1996; Reg. Y, 62 FR 9343, Feb. 28, 1997]

§ 225.126 Activities not closely related to banking.

Pursuant to section 4(c)(8) of the Bank Holding Company Act and § 225.4(a) of Regulation Y, the Board of Governors has determined that the following activities are not so closely related to banking or managing or controlling banks as to be a proper incident thereto:

(a) Insurance premium funding—that is, the combined sale of mutual funds and insurance.

(b) Underwriting life insurance that is not sold in connection with a credit transaction by a bank holding company, or a subsidiary thereof.

(c) Real estate brokerage (see 1972 Fed. Res. Bulletin 428).

(d) Land development (see 1972 Fed. Res. Bulletin 429).

(e) Real estate syndication.

(f) Management consulting (see 1972 Fed. Res. Bulletin 571).

(g) Property management (see 1972 Fed. Res. Bulletin 652).

[Reg. Y, 37 FR 20329, Sept. 29, 1972; 37 FR 21938, Oct. 17, 1972, as amended at 54 FR 37302, Sept. 8, 1989]

§ 225.127 Investment in corporations or projects designed primarily to promote community welfare.

(a) Under § 225.25(b)(6) of Regulation Y, a bank holding company may, in accordance with the provisions of § 225.23, engage in ''making equity and debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas.'' The Board included that activity among those the Board has determined to be so closely related to banking or managing or controlling banks as be a proper incident thereto, in order to permit bank holding companies to fulfill their civic responsibilities. As indicated hereinafter in this interpretation, the Board intends § 225.25(b)(6) to enable bank holding companies to take an active role in the quest for solutions to the Nation's social problems. Although the interpretation primarily focuses on low- and moderate-income housing, it is not intended to limit projects under § 225.25(b)(6) to that area. Other investments primarily designed to promote community welfare are considered permissible, but have not been defined in order to provide bank holding companies flexibility in approaching community problems. For example, bank holding companies may utilize this flexibility to provide new and creative approaches to the promotion of employment opportunities for low-income persons. Bank holding companies possess a unique combination of financial and managerial resources making them particularly suited for a meaningful and substantial role in remedying our social ills. Section 225.25(b)(6) is intended to provide an opportunity for them to assume such a role.

(b) Under the authority of § 225.25(b)(6), a bank holding company may invest in community development corporations established pursuant to Federal or State law. A bank holding company may also participate in other civic projects, such as a municipal parking facility sponsored by a local civic organization as a means to promote greater public use of the community's facilities.

(c) Within the category of permissible investments under § 225.25(b)(6)

are investments in projects to construct or rehabilitate multifamily low- or moderate-income housing with respect to which a mortgage is insured under section 221(d)(3), 221(d)(4), or 236 of the National Housing Act (12 U.S.C. 1701) and investments in projects to construct or rehabilitate low- or moderate-income housing which is financed or assisted by direct loan, tax abatement, or insurance under provisions of State or local law, similar to the aforementioned Federal programs, provided that, with respect to all such projects the owner is, by statute, regulation, or regulatory authority, limited as to the rate of return on his investment in the project, as to rentals or occupancy charges for units in the project, and in such other respects as would be a ''limited dividend corporation'' (as defined by the Secretary of Housing and Urban Development).

(d) Investments in other projects that may be considered to be designed primarily to promote community welfare include but are not limited to: (1) Projects for the construction or rehabilitation of housing for the benefit of persons of low- or moderate-income, (2) projects for the construction or rehabilitation of ancillary local commercial facilities necessary to provide goods or services principally to persons residing in low- or moderate-income housing, and (3) projects designed explicitly to create improved job opportunities for low- or moderate-income groups (for example, minority equity investments, on a temporary basis, in small or medium-sized locally-controlled businesses in low-income urban or other economically depressed areas). In the case of de novo projects, the copy of the notice with respect to such other projects which is to be furnished to Reserve Banks in accordance with the provisions of §225.23 should be accompanied by a memorandum which demonstrates that such projects meet the objectives of §225.25(b)(6).

(e) Investments in corporations or projects organized to build or rehabilitate high-income housing, or commercial, office, or industrial facilities that are not designed explicitly to create improved job opportunities for low-income persons shall be presumed not to be designed primarily to promote community welfare, unless there is substantial evidence to the contrary, even though to some extent the investment may benefit the community.

(f) Section 6 of the Depository Institutions Disaster Relief Act of 1992 permits state member banks (12 U.S.C. 338a) and national banks (12 U.S.C. 24 (Eleventh)) to invest in the stock of community development corporations that are designed primarily to promote the public welfare of low- and moderate-income communities and persons in the areas of housing, services and employment. The Board and the Office of the Comptroller of the Currency have adopted rules that permit state member banks and national banks to make certain investments without prior approval. The Board believes that these rules are consistent with the Board's interpretation of, and decisions regarding, the scope of community welfare activities permissible for bank holding companies. Accordingly, approval received by a bank holding company to conduct activities designed to promote the community welfare under section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1843(c)(8)) and §225.25(b)(6) of the Board's Regulation Y (12 CFR 225.25(b)(6)) includes approval to engage, either directly or through a subsidiary, in the following activities, up to five percent of the bank holding company's total consolidated capital stock and surplus, without additional Board or Reserve Bank approval:

(1) Invest in and provide financing to a corporation or project or class of corporations or projects that the Board previously has determined is a public welfare project pursuant to paragraph 23 of section 9 of the Federal Reserve Act (12 U.S.C. 338a);

(2) Invest in and provide financing to a corporation or project that the Office of the Comptroller of the Currency previously has determined, by order or regulation, is a public welfare investment pursuant to section 5136 of the Revised Statutes (12 U.S.C. 24 (Eleventh));

(3) Invest in and provide financing to a community development financial institution pursuant to section 103(5) of the Community Development Banking

and Financial Institutions Act of 1994 (12 U.S.C. 4702(5));

(4) Invest in, provide financing to, develop, rehabilitate, manage, sell, and rent residential property if a majority of the units will be occupied by low- and moderate-income persons or if the property is a ''qualified low-income building'' as defined in section 42(c)(2) of the Internal Revenue Code (26 U.S.C. 42(c)(2));

(5) Invest in, provide financing to, develop, rehabilitate, manage, sell, and rent nonresidential real property or other assets located in a low- or moderate-income area provided the property is used primarily for low- and moderate-income persons;

(6) Invest in and provide financing to one or more small businesses located in a low- or moderate-income area to stimulate economic development;

(7) Invest in, provide financing to, develop, and otherwise assist job training or placement facilities or programs designed primarily for low- and moderate-income persons;

(8) Invest in and provide financing to an entity located in a low- or moderate-income area if that entity creates long-term employment opportunities, a majority of which (based on full time equivalent positions) will be held by low- and moderate-income persons; and

(9) Provide technical assistance, credit counseling, research, and program development assistance to low- and moderate-income persons, small businesses, or nonprofit corporations to help achieve community development.

(g) For purposes of paragraph (f) of this section, low- and moderate-income persons or areas means individuals and communities whose incomes do not exceed 80 percent of the median income of the area involved, as determined by the U.S. Department of Housing and Urban Development. Small businesses are businesses that are smaller than the maximum size eligibility standards established by the Small Business Administration (SBA) for the Small Business Investment Company and Development Company Programs or the SBA section 7A loan program; and specifically include those businesses that are majority-owned by members of minority groups or by women.

(h) For purposes of paragraph (f) of this section, five percent of the total consolidated capital stock and surplus of a bank holding company includes its total investment in projects described in paragraph (f) of this section, when aggregated with similar types of investments made by depository institutions controlled by the bank holding company. The term total consolidated capital stock and surplus of the bank holding company means total equity capital and the allowance for loan and lease losses. For bank holding companies that file the FR Y–9C (Consolidated Financial Statements for Bank Holding Companies), these items are readily ascertained from Schedule HC—Consolidated Balance Sheet (total equity capital (line 27h) and allowance for loan and lease losses (line 4b)). For bank holding companies filing the FR Y-SP (Parent Company Only Financial Statements for Small Bank Holding Companies), an approximation of these items is ascertained from the Balance Sheet (total equity capital (line 16e)) and allowance for loan and lease losses (line 3b)) and from the Report of Condition for Insured Banks (Schedule RC—Balance Sheet (line 4b)).

[37 FR 11316, June 7, 1972; 37 FR 13336, July 7, 1972, as amended at Reg. Y, 59 FR 63713, Dec. 9, 1994]

§ 225.129 Activities closely related to banking.

Courier activities. The Board's amendment of § 225.4(a), which adds courier services to the list of closely related activities is intended to permit holding companies to transport time critical materials of limited intrinsic value of the types utilized by banks and bank-related firms in performing their business activities. Such transportation activities are of particular importance in the check clearing process of the banking system, but are also important to the performance of other activities, including the processing of financially-related economic data. The authority is not intended to permit holding companies to engage generally in the provision of transportation services.

During the course of the Board's proceedings pertaining to courier services,

objections were made that courier activities were not a proper incident to banking because of the possibility that holding companies would or had engaged in unfair competitive practices. The Board believes that adherence to the following principles will eliminate or reduce to an insignificant degree any possibility of unfair competition:

a. A holding company courier subsidiary established under section 4(c)(8) should be a separate, independent corporate entity, not merely a servicing arm of a bank.

b. As such, the subsidiary should exist as a separate, profit-oriented operation and should not be subsidized by the holding company system.

c. Services performed should be explicitly priced, and shall not be paid for indirectly, for example, on the basis of deposits maintained at or loan arrangements with affiliated banks.

Accordingly, entry of holding companies into courier activities on the basis of section 4(c)(8) will be conditioned as follows:

1. *The courier subsidiary shall perform services on an explicit fee basis and shall be structured as an individual profit center designed to be operated on a profitable basis.* The Board may regard operating losses sustained over an extended period as being inconsistent with continued authority to engage in courier activities.

2. *Courier services performed on behalf of an affiliate's customer* (*such as the carriage of incoming cash letters*) *shall be paid for by the customer. Such payments shall not be made indirectly, for example, on the basis of imputed earnings on deposits maintained at or of loan arrangements with subsidiaries of the holding company.* Concern has also been expressed that bank-affiliated courier services will be utilized to gain a competitive advantage over firms competing with other holding company affiliates. To reduce the possibility that courier affiliates might be so employed, the Board will impose the following third condition:

3. *The courier subsidiary shall, when requested by any bank or any data processing firm providing financially-related data processing services which firm competes with a banking or data processing* subsidiary of Applicant, furnish comparable service at comparable rates, unless compliance with such request would be beyond the courier subsidiary's practical capacity. In this regard, the courier subsidiary should make known to the public its minimum rate schedule for services and its general pricing policies thereto. The courier subsidiary is also expected to maintain for a reasonable period of time (not less than two years) each request denied with the reasons for such denial.

[38 FR 32126, Nov. 21, 1973, as amended at 40 FR 36309, Aug. 20, 1975]

§ 225.130 Issuance and sale of short-term debt obligations by bank holding companies.

For text of interpretation, see § 250.221 of this chapter.

[38 FR 35231, Dec. 26, 1973]

§ 225.131 Activities closely related to banking.

(a) *Bank management consulting advice.* The Board's amendment of § 225.4(a), which adds bank management consulting advice to the list of closely related activities, described in general terms the nature of such activity. This interpretation is intended to explain in greater detail certain of the terms in the amendment.

(b) It is expected that bank management consulting advice would include, but not be limited to, advice concerning: Bank operations, systems and procedures; computer operations and mechanization; implementation of electronic funds transfer systems; site planning and evaluation; bank mergers and the establishment of new branches; operation and management of a trust department; international banking; foreign exchange transactions; purchasing policies and practices; cost analysis, capital adequacy and planning; auditing; accounting procedures; tax planning; investment advice (as authorized in § 225.4(a)(5)); credit policies and administration, including credit documentation, evaluation, and debt collection; product development, including specialized lending provisions; marketing operations, including research, market development and advertising programs; personnel operations,

including recruiting, training, evaluation and compensation; and security measures and procedures.

(c) In permitting bank holding companies to provide management consulting advice to nonaffiliated ''banks'', the Board intends such advice to be given only to an institution that both accepts deposits that the depositor has a legal right to withdraw on demand and engages in the business of making commercial loans. It is also intended that such management consulting advice may be provided to the ''operations subsidiaries'' of a bank, since such subsidiaries perform functions that a bank is empowered to perform directly at locations at which the bank is authorized to engage in business (§ 250.141 of this chapter).

(d) Although a bank holding company providing management consulting advice is prohibited by the regulation from owning or controlling, directly or indirectly, any equity securities in a client bank, this limitation does not apply to shares of a client bank acquired, directly or indirectly, as a result of a default on a debt previously contracted. This limitation is also inapplicable to shares of a client bank acquired by a bank holding company, directly or indirectly, in a fiduciary capacity: *Provided,* That the bank holding company or its subsidiary does not have sole discretionary authority to vote such shares or shares held with sole voting rights constitute not more than five percent of the outstanding voting shares of a client bank.

[39 FR 8318, Mar. 5, 1974; 39 FR 21120, June 19, 1974]

§ 225.132 Acquisition of assets.

(a) From time to time questions have arisen as to whether and under what circumstances a bank holding company engaged in nonbank activities, directly or indirectly through a subsidiary, pursuant to section 4(c)(8) of the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1843(c)(3)), may acquire the assets and employees of another company, without first obtaining Board approval pursuant to section 4(c)(8) and the Board's Regulation Y (12 CFR 225.4(b)).

(b) In determining whether Board approval is required in connection with the acquisition of assets, it is necessary to determine (a) whether the acquisition is made in the ordinary course of business[1] or (b) whether it constitutes the acquisition, in whole or in part, of a going concern.[2]

(c) The following examples illustrate transactions where prior Board approval will generally be required:

(1) The transaction involves the acquisition of all or substantially all of the assets of a company, or a subsidiary, division, department or office thereof.

(2) The transaction involves the acquisition of less than ''substantially all'' of the assets of a company, or a subsidiary, division, department or office thereof, the operations of which are being terminated or substantially discontinued by the seller, but such asset acquisition is significant in relation to the size of the same line of nonbank activity of the holding company (e.g., consumer finance mortgage banking, data processing). For purposes of this interpretation, an acquisition would generally be presumed to be significant if the book value of the nonbank assets being acquired exceeds 50 percent of the book value of the nonbank assets of the holding company or nonbank subsidiary comprising the same line of activity.

(3) The transaction involves the acquisition of assets for resale and the sale of such assets is not a normal business activity of the acquiring holding company.

(4) The transaction involves the acquisition of the assets of a company, or a subsidiary, division, department or office thereof, and a major purpose of the transaction is to hire some of the seller's principal employees who are expert, skilled and experienced in the

[1] Section 225.4(c)(3) of the Board's Regulation Y (12 CFR 225.4(c)(3)) generally prohibits a bank holding company or its subsidiary engaged in activities pursuant to authority of section 4(c)(8) of the Act from being a party to any merger ''or acquisition of assets other than in the ordinary course of business'' without prior Board approval.

[2] In accordance with the provisions of section 4(c)(8) of the Act and § 225.4(b) of Regulation Y, the acquisition of a going concern requires prior Board approval.

business of the company being acquired.

(d) In some cases it may be difficult, due to the wide variety of circumstances involving possible acquisition of assets, to determine whether such acquisitions require prior Board approval. Bank holding companies are encouraged to contact their local Reserve Bank for guidance where doubt exists as to whether such an acquisition is in the ordinary course of business or an acquisition, in whole or in part, of a going concern.

[39 FR 35128, Sept. 30, 1974, as amended at Reg. Y, 57 FR 28779, June 29, 1992]

§ 225.133 Computation of amount invested in foreign corporations under general consent procedures.

For text of this interpretation, see § 211.111 of this subchapter.

[40 FR 43199, Sept. 19, 1975]

§ 225.134 Escrow arrangements involving bank stock resulting in a violation of the Bank Holding Company Act.

(a) In connection with a recent application to become a bank holding company, the Board considered a situation in which shares of a bank were acquired and then placed in escrow by the applicant prior to the Board's approval of the application. The facts indicated that the applicant company had incurred debt for the purpose of acquiring bank shares and immediately after the purchase the shares were transferred to an unaffiliated escrow agent with instructions to retain possession of the shares pending Board action on the company's application to become a bank holding company. The escrow agreement provided that, if the application were approved by the Board, the escrow agent was to return the shares to the applicant company; and, if the application were denied, the escrow agent was to deliver the shares to the applicant company's shareholders upon their assumption of debt originally incurred by the applicant in the acquisition of the bank shares. In addition, the escrow agreement provided that, while the shares were held in escrow, the applicant could not exercise voting or any other ownership rights with respect to those shares.

(b) On the basis of the above facts, the Board concluded that the company had violated the prior approval provisions of section 3 of the Bank Holding Company Act (''Act'') at the time that it made the initial acquisition of bank shares and that, for purposes of the Act, the company continued to control those shares in violation of the Act. In view of these findings, individuals and bank holding companies should not enter into escrow arrangements of the type described herein, or any similar arrangement, without securing the prior approval of the Board, since such action could constitute a violation of the Act.

(c) While the above represents the Board's conclusion with respect to the particular escrow arrangement involved in the proposal presented, the Board does not believe that the use of an escrow arrangement would always result in a violation of the Act. For example, it appears that a transaction whereby bank shares are placed in escrow pending Board action on an application would not involve a violation of the Act so long as title to such shares remains with the seller during the pendency of the application; there are no other indicia that the applicant controls the shares held in escrow; and, in the event of a Board denial of the application, the escrow agreement provides that the shares would be returned to the seller.

[41 FR 9859, Mar. 8, 1976. Correctly designated at 41 FR 12009, Mar. 23, 1976]

§ 225.136 Utilization of foreign subsidiaries to sell long-term debt obligations in foreign markets and to transfer the proceeds to their United States parent(s) for domestic purposes.

For text of this interpretation, see § 211.112 of this subchapter.

[42 FR 752, Jan. 4, 1977]

§ 225.137 Acquisitions of shares pursuant to section 4(c)(6) of the Bank Holding Company Act.

(a) The Board has received a request for an interpretation of section 4(c)(6) of the Bank Holding Company Act

(''Act'')[1] in connection with a proposal under which a number of bank holding companies would purchase interests in an insurance company to be formed for the purpose of underwriting or reinsuring credit life and credit accident and health insurance sold in connection with extensions of credit by the stockholder bank holding companies and their affiliates.

(b) Each participating holding company would own no more than 5 percent of the outstanding voting shares of the company. However, the investment of each holding company would be represented by a separate class of voting security, so that each stockholder would own 100 percent of its respective class. The participating companies would execute a formal ''Agreement Among Stockholders'' under which each would agree to use its best efforts at all times to direct or recommend to customers and clients the placement of their life, accident and health insurance directly or indirectly with the company. Such credit-related insurance placed with the company would be identified in the records of the company as having been originated by the respective stockholder. A separate capital account would be maintained for each stockholder consisting of the original capital contribution increased or decreased from time to time by the net profit or loss resulting from the insurance business attributable to each stockholder. Thus, each stockholder would receive a return on its investment based upon the claims experience and profitability of the insurance business that it had itself generated. Dividends declared by the board of directors of the company would be payable to each stockholder only out of the earned surplus reflected in the respective stockholder's capital account.

(c) It has been requested that the Board issue an interpretation that section 4(c)(6) of the Act provides an exemption under which participating bank holding companies may acquire such interests in the company without prior approval of the Board.

(d) On the basis of a careful review of the documents submitted, in light of the purposes and provisions of the Act, the Board has concluded that section 4(c)(6) of the Act is inapplicable to this proposal and that a bank holding company must obtain the approval of the Board before participating in such a proposal in the manner described. The Board's conclusion is based upon the following considerations:

(1) Section 2(a)(2)(A) of the Act provides that a company is deemed to have control over a second company if it owns or controls ''25 per centum or more of any class of voting securities'' of the second company. In the case presented, the stock interest of each participant would be evidenced by a different class of stock and each would accordingly, own 100 percent of a class of voting securities of the company. Thus, each of the stockholders would be deemed to ''control'' the company and prior Board approval would be required for each stockholder's acquisition of stock in the company.

The Board believes that this application of section 2(a)(2)(A) of the Act is particularly appropriate on the facts presented here. The company is, in practical effect, a conglomeration of separate business ventures each owned 100 percent by a stockholder the value of whose economic interest in the company is determined by reference to the profits and losses attributable to its respective class of stock. Furthermore, it is the Board's opinion that this application of section 2(a)(2)(A) is not inconsistent with section 4(c)(6). Even assuming that section (4)(c)(6) is intended to refer to all outstanding voting shares, and not merely the outstanding shares of a particular class of securities, section 4(c)(6) must be viewed as permitting ownership of 5 percent of a company's voting stock only when that ownership does not

[1] It should be noted that every Board Order granting approval under section 4(c)(8) of the Act contains the following paragraph:

''This determination is subject . . . to the Board's authority to require such modification or termination of the activities of a holding company or any of its subsidiaries as the Board finds necessary to assure compliance with the provisions and purposes of the Act and the Board's regulations and orders issued thereunder, or to prevent evasion thereof.''

The Board believes that, even apart from this Interpretation, this language preserves the authority of the Board to require the revisions contemplated in this Interpretation.

constitute ''control'' as otherwise defined in the Act. For example, it is entirely possible that a company could exercise a controlling influence over the management and policies of a second company, and thus ''control'' that company under the Act's definitions, even though it held less than 5 percent of the voting stock of the second company. To view section 4(c)(6) as an unqualified exemption for holdings of less than 5 percent would thus create a serious gap in the coverage of the Act.

(2) The Board believes that section 4(c)(6) should properly be interpreted as creating an exemption from the general prohibitions in section 4 on ownership of stock in nonbank companies only for passive investments amounting to not more than 5 percent of a company's outstanding stock, and that the exemption was not intended to allow a group of holding companies, through concerted action, to engage in an activity as entrepreneurs. Section 4 of the Act, of course, prohibits not only owning stock in nonbank companies, but engaging in activities other than banking or those activities permitted by the Board under section 4(c)(8) as being closely related to banking. Thus, if a holding company may be deemed to be engaging in an activity through the medium of a company in which it owns less than 5 percent of the voting stock it may nevertheless require Board approval, despite the section 4(c)(6) exemption.

(e) To accept the argument that section 4(c)(6) is an unqualified grant of permission to a bank holding company to own 5 percent of the shares of any nonbanking company irrespective of the nature or extent of the holding company's participation in the affairs of the nonbanking company would, in the Board's view, create the potential for serious and widespread evasion of the Act's controls over nonbanking activities. Such a construction would allow a group of 20 bank holding companies—or even a single bank holding company and one or more nonbank companies—to engage in entrepreneurial joint ventures in businesses prohibited to bank holding companies, a result the Board believes to be contrary to the intent of Congress.

(f) In this proposal, each of the participating stockholders must be viewed as engaging in the business of insurance underwriting. Each stockholder would agree to channel to the company the insurance business it generates, and the value of the interest of each stockholder would be determined by reference to the profitability of the business generated by that stockholder itself. There is no sharing or pooling among stockholders of underwriting risks assumed by the company, and profit or loss from investments is allocated on the basis of each bank holding company's allocable underwriting profit or loss. The interest of each stockholder is thus clearly that of an entrepreneur rather than that of an investor.

(g) Accordingly, on the basis of the factual situation before the Board, and for the reasons summarized above, the Board has concluded that section 4(c)(6) of the Act cannot be interpreted to exempt the ownership of 5 percent of the voting stock of a company under the circumstances described, and that a bank holding company wishing to become a stockholder in a company under this proposal would be required to obtain the Board's approval to do so.

[42 FR 1263, Jan. 6, 1977; 42 FR 2951, Jan. 14, 1977]

§ 225.138 Statement of policy concerning divestitures by bank holding companies.

(a) From time to time the Board of Governors receives requests from companies subject to the Bank Holding Company Act, or other laws administered by the Board, to extend time periods specified either by statute or by Board order for the divestiture of assets held or activities engaged in by such companies. Such divestiture requirements may arise in a number of ways. For example, divestiture may be ordered by the Board in connection with an acquisition found to have been made in violation of law. In other cases the divestiture may be pursuant to a statutory requirement imposed at the time and amendment to the Act was adopted, or it may be required as a result of a foreclosure upon collateral

held by the company or a bank subsidiary in connection with a debt previously contracted in good faith. Certain divestiture periods may be extended in the discretion of the Board, but in other cases the Board may be without statutory authority, or may have only limited authority, to extend a specified divestiture period.

(b) In the past, divestitures have taken many different forms, and the Board has followed a variety of procedures in enforcing divestiture requirements. Because divestitures may occur under widely disparate factual circumstances, and because such forced dispositions may have the potential for causing a serious adverse economic impact upon the divesting company, the Board believes it is important to maintain a large measure of flexibility in dealing with divestitures. For these reasons, there can be no fixed rule as to the type of divestiture that will be appropriate in all situations. For example, where divestiture has been ordered to terminate a control relationship created or maintained in violation of the Act, it may be necessary to impose conditions that will assure that the unlawful relationship has been fully terminated and that it will not arise in the future. In other circumstances, however, less stringent conditions may be appropriate.

(1) *Avoidance of delays in divestitures.* Where a specific time period has been fixed for accomplishing divestiture, the affected company should endeavor and should be encouraged to complete the divestiture as early as possible during the specific period. There will generally be substantial advantages to divesting companies in taking steps to plan for and accomplish divestitures well before the end of the divestiture period. For example, delays may impair the ability of the company to realize full value for the divested assets, for as the end of the divestiture period approaches the ''forced sale'' aspect of the divestiture may lead potential buyers to withhold firm offers and to bargain for lower prices. In addition, because some prospective purchasers may themselves require regulatory approval to acquire the divested property, delay by the divesting company may—by leaving insufficient time to obtain such approvals—have the effect of narrowing the range of prospective purchases. Thus, delay in planning for divestiture may increase the likelihood that the company will seek an extension of the time for divestiture if difficulty is encountered in securing a purchaser, and in certain situations, of course, the Board may be without statutory authority to grant extensions.

(2) *Submissions and approval of divestiture plans.* When a divestiture requirement is imposed, the company affected should generally be asked to submit a divestiture plan promptly for review and approval by the Reserve Bank or the Board. Such a requirement may be imposed pursuant to the Board's authority under section 5(b) of the Bank Holding Company Act to issue such orders as may be necessary to enable the Board to administer and carry out the purposes of the Act and prevent evasions thereof. A divestiture plan should be as specific as possible, and should indicate the manner in which divestiture will be accomplished—for example, by a bulk sale of the assets to a third party, by ''spinoff'' or distribution of shares to the shareholders of the divesting company, or by termination of prohibited activities. In addition, the plan should specify the steps the company expects to take in effecting the divestiture and assuring its completeness, and should indicate the time schedule for taking such steps. In appropriate circumstances, the divestiture plan should make provision for assuring that ''controlling influence'' relationships, such as management or financial interlocks, will not continue to exist.

(3) *Periodic progress reports.* A company subject to a divestiture requirement should generally be required to submit regular periodic reports detailing the steps it has taken to effect divestiture. Such a requirement may be imposed pursuant to the Board's authority under section 5(b) of the Bank Holding Company Act, referred to above, as well as its authority under section 5(c) of the Act to require reports for the purpose of keeping the Board informed as to whether the Act and Board regulations and order thereunder are being complied with. Reports should set forth in detail such matters

as the identities of potential buyers who have been approached by the company, the dates of discussions with potential buyers and the identities of the individuals involved in such discussions, the terms of any offers received, and the reasons for rejecting any offers. In addition, the reports should indicate whether the company has employed brokers, investment bankers or others to assist in the divestiture, or its reasons for not doing so, and should describe other efforts by the company to seek out possible purchasers. The purpose of requiring such reports is to insure that substantial and good faith efforts being made by the company to satisfy its divestiture obligations. The frequency of such reports may vary depending upon the nature of the divestiture and the period specified for divestiture. However, such reports should generally not be required less frequently than every three months, and may in appropriate cases be required on a monthly or even more frequent basis. Progress reports as well as divestiture plans should be afforded confidential treatment.

(4) *Extensions of divestiture periods.* Certain divestiture periods—such as December 31, 1980 deadline for divestitures required by the 1970 Amendments to the Bank Holding Company Act—are not extendable. In such cases it is imperative that divestiture be accomplished in a timely manner. In certain other cases, the Board may have discretion to extend a statutorily prescribed divestiture period within specified limits. For example, under section 4(c)(2) of the Act the Board may extend for three one-year periods the two-year period in which a bank subsidiary of a holding company is otherwise required to divest shares acquired in satisfaction of a debt previously contracted in good faith. In such cases, however, when the permissible extensions expire the Board no longer has discretion to grant further extensions. In still other cases, where a divestiture period is prescribed by the Board, in the exercise of its regulatory judgment, the Board may have broader discretion to grant extensions. Where extensions of specified divestiture periods are permitted by law, extensions should not be granted except under compelling circumstances. Neither unfavorable market conditions, nor the possibility that the company may incur some loss, should alone be viewed as constituting such circumstances—particularly if the company has failed to take earlier steps to accomplish a divestiture under more favorable circumstances. Normally, a request for an extension will not be considered unless the company has established that it has made substantial and continued good faith efforts to accomplish the divestiture within the prescribed period. Furthermore, requests for extensions of divestiture periods must be made sufficiently in advance of the expiration of the prescribed period both to enable the Board to consider the request in an orderly manner and to enable the company to effect a timely divestiture in the event the request for extension is denied. Companies subject to divestiture requirements should be aware that a failure to accomplish a divestiture within the prescribed period may in and of itself be viewed as a separate violation of the Act.

(5) *Use of trustees.* In appropriate cases a company subject to a divestiture requirement may be required to place the assets subject to divestiture with an independent trustee under instructions to accomplish a sale by a specified date, by public auction if necessary. Such a trustee may be given the responsibility for exercising the voting rights with respect to shares being divested. The use of such a trustee may be particularly appropriate where the divestiture is intended to terminate a control relationship established or maintained in violation of law, or where the divesting company has demonstrated an inability or unwillingness to take timely steps to effect a divestiture.

(6) *Presumptions of control.* Bank holding companies contemplating a divestiture should be mindful of section 2(g)(3) of the Bank Holding Company Act, which creates a presumption of continued control over the transferred assets where the transferee is indebted to the transferor, or where certain interlocks exist, as well as §225.2 of Regulation Y, which sets forth certain additional control presumptions. Where one of these presumptions has

arisen with respect to divested assets, the divestiture will not be considered as complete until the presumption has been overcome. It should be understood that the inquiry into the termination of control relationships is not limited by the statutory and regulatory presumptions of control, and that the Board may conclude that a control relationship still exists even though the presumptions do not apply.

(7) *Role of the Reserve Banks.* The Reserve Banks have a responsibility for supervising and enforcing divestitures. Specifically, in coordination with Board staff they should review divestiture plans to assure that proposed divestitures will result in the termination of control relationships and will not create unsafe or unsound conditions in any bank or bank holding company; they should monitor periodic progress reports to assure that timely steps are being taken to effect divestitures; and they should prompt companies to take such steps when it appears that progress is not being made. Where Reserve Banks have delegated authority to extend divestiture periods, that authority should be exercised consistently with this policy statement.

[42 FR 10969, Feb. 25, 1977]

§ 225.139 Presumption of continued control under section 2(g)(3) of the Bank Holding Company Act.

(a) Section 2(g)(3) of the Bank Holding Company Act (the ''Act'') establishes a statutory presumption that where certain specified relationships exist between a transferor and transferee of shares, the transferor (if it is a bank holding company, or a company that would be such but for the transfer) continues to own or control indirectly the transferred shares.[1] This presumption arises by operation of law, as of the date of the transfer, without the need for any order or determination by the Board. Operation of the presumption may be terminated only by the issuance of a Board determination, after opportunity for hearing, ''that the transferor is not in fact capable of controlling the transferee.''[2]

(b) The purpose of section 2(g)(3) is to provide the Board an opportunity to assess the effectiveness of divestitures in certain situations in which there may be a risk that the divestiture will not result in the complete termination of a control relationship. By presuming control to continue as a matter of law, section 2(g)(3) operates to allow the effectiveness of the divestiture to be assessed before the divesting company is permitted to act on the assumption that the divestiture is complete. Thus, for example, if a holding company divests its banking interest under circumstances where the presumption of continued control arises, the divesting company must continue to consider itself bound by the Act until an appropriate order is entered by the Board dispelling the presumption. Section 2(g)(3) does not establish a substantive rule that invalidates transfers to which it applies, and in a great many cases the Board has acted favorably on applications to have the presumption dispelled. It merely provides a procedural opportunity for Board consideration of the effect of such transfers in advance of their being deemed effective. Whether or not the statutory presumption arises, the substantive test for assessing the effectiveness of a divestiture is the same—that is, the Board must be assured that all control relationships between the transferor and the transferred property have been terminated and will not be reestablished.[3]

[1] The presumption arises where the transferee ''is indebted to the transferor, or has one or more officers, directors, trustees, or beneficiaries in common with or subject to control by the transferor.''

[2] The Board has delegated to its General Counsel the authority to issue such determinations, 12 CFR 265.2(b)(1).

[3] It should be noted, however, that the Board will require termination of any interlocking management relationships between the divesting company and the transferee or the divested company as a precondition of finding that a divestiture is complete. Similarly, the retention of an economic interest in the divested company that would create an incentive for the divesting company to attempt to influence the management of the divested company will preclude a finding that the divestiture is complete. (See the Board's Order in the matter of ''International Bank'', 1977 Federal Reserve Bulletin 1106, 1113.)

(c) In the course of administering section 2(g)(3) the Board has had several occasions to consider the scope of that section. In addition, questions have been raised by and with the Board's staff as to coverage of the section. Accordingly, the Board believes it would be useful to set forth the following interpretations of section 2(g)(3):

(1) The terms *transferor* and *transferee,* as used in section 2(g)(3), include parents and subsidiaries of each. Thus, for example, where a transferee is indebted to a subsidiary of the transferor, or where a specified interlocking relationship exists between the transferor or transferee and a subsidiary of the other (or between subsidiaries of each), the presumption arises. Similarly, if a parent of the transferee is indebted to a parent of the transferor, the presumption arises. The presumption of continued control also arises where an interlock or debt relationship is retained between the divesting company and the company being divested, since the divested company will be or may be viewed as a *subsidiary* of the transferee or group of transferees.

(2) The terms *officers, directors,* and *trustees,* as used in section 2(g)(3), include persons performing functions normally associated with such positions (including general partners in a partnership and limited partners having a right to participate in the management of the affairs of the partnership) as well as persons holding such positions in an advisory or honorary capacity. The presumption arises not only where the transferee or transferred company has an officer, director or trustee *in common with* the transferor, but where the transferee himself holds such a position with the transferor.[4] It should be noted that where a transfer takes the form of a pro-rata distribution, or *spin-off,* of shares to a company's shareholders, officers and directors of the transferor company are likely to receive a portion of such shares. The presumption of continued control would, of course, attach to any shares transferred to officers and directors of the divesting company, whether by *spinoff* or outright sale. However, the presumption will be of legal significance—and will thus require an application under section 2(g)(3)—only where the total number of shares subject to the presumption exceeds one of the applicable thresholds in the Act. For example, where officers and directors of a one-bank holding company receive in the aggregate 25 percent or more of the stock of a bank subsidiary being divested by the holding company, the holding company would be presumed to continue to control the *divested* bank. In such a case it would be necessary for the divesting company to demonstrate that it no longer controls either the divested bank or the officer/director transferees. However, if officers and directors were to receive in the aggregate less than 25 percent of the bank's stock (and no other shares were subject to the presumption), section 2(g)(3) would not have the legal effect of presuming continued control of the bank.[5] In the case of a divestiture of nonbank shares, an application under section 2(g)(3) would be required whenever officers and directors of the divesting company received in the aggregate more than 5 percent of the shares of the company being divested.

(3) Although section 2(g)(3) refers to transfers of *shares* it is not, in the Board's view, limited to disposition of corporate stock. General or limited partnership interests, for example, are included within the term *shares.* Furthermore, the transfer of all or substantially all of the assets of a company, or the transfer of such a significant volume of assets that the transfer may in effect constitute the disposition

[4] It has been suggested that the words *in common with* in section 2(g)(3) evidence an intent to make the presumption applicable only where the transferee is a *company* having an interlock with the transferor. Such an interpretation would, in the Board's view, create an unwarranted gap in the coverage of section 2(g)(3). Furthermore, because the presumption clearly arises where the transferee is an individual who is indebted to the transferor such an interpretation would result in an illogical internal inconsistency in the statute.

[5] Of course, the fact that section 2(g)(3) would not operate to presume continued control would not necessarily mean that control had in fact been terminated if control could be exercised through other means.

of a separate activity of the company, is deemed by the Board to involve a transfer of *shares* of that company.

(4) The term *indebtedness* giving rise to the presumption of continued control under section 2(g)(3) of the Act is not limited to debt incurred in connection with the transfer; it includes any debt outstanding at the time of transfer from the transferee to the transferor or its subsidiaries. However, the Board believes that not every kind of indebtedness was within the contemplation of the Congress when section 2(g)(3) was adopted. Routine business credit of limited amounts and loans for personal or household purposes are generally not the kinds of indebtedness that, standing alone, support a presumption that the creditor is able to control the debtor. Accordingly, the Board does not regard the presumption of section 2(g)(3) as applicable to the following categories of credit, provided the extensions of credit are not secured by the transferred property and are made in the ordinary course of business of the transferor (or its subsidiary) that is regularly engaged in the business of extending credit:

(i) Consumer credit extended for personal or household use to an individual transferee; (ii) student loans made for the education of the individual transferee or a spouse or child of the transferee; (iii) a home mortgage loan made to an individual transferee for the purchase of a residence for the individual's personal use and secured by the residence; and (iv) loans made to companies (as defined in section 2(b) of the Act) in an aggregate amount not exceeding ten per cent of the total purchase price (or if not sold, the fair market value) of the transferred property. The amounts and terms of the preceding categories of credit should not differ substantially from similar credit extended in comparable circumstances to others who are not transferees. It should be understood that, while the statutory presumption in situations involving these categories of credit may not apply, the Board is not precluded in any case from examining the facts of a particular transfer and finding that the divestiture of control was ineffective based on the facts of record.

(d) Section 2(g)(3) provides that a Board determination that a transferor is not in fact capable of controlling a transferee shall be made after opportunity for hearing. It has been the Board's routine practice since 1966 to publish notice in the FEDERAL REGISTER of applications filed under section 2(g)(3) and to offer interested parties an opportunity for a hearing. Virtually without exception no comments have been submitted on such applications by parties other than the applicant and, with the exception of one case in which the request was later withdrawn, no hearings have been requested in such cases. Because the Board believes that the hearing provision in section 2(g)(3) was intended as a protection for applicants who are seeking to have the presumption overcome by a Board order, a hearing would not be of use where an application is to be granted. In light of the experience indicating that the publication of FEDERAL REGISTER notice of such applications has not served a useful purpose, the Board has decided to alter its procedures in such cases. In the future, FEDERAL REGISTER notice of section 2(g)(3) applications will be published only in cases in which the Board's General Counsel, acting under delegated authority, has determined not to grant such an application and has referred the matter to the Board for decision.[6]

(12 U.S.C. 1841, 1844)

[43 FR 6214, Feb. 14, 1978; 43 FR 15147, Apr. 11, 1978; 43 FR 15321, Apr. 12, 1978, as amended at 45 FR 8280, Feb. 7, 1980; 45 FR 11125, Feb. 20, 1980]

§ 225.140 Disposition of property acquired in satisfaction of debts previously contracted.

(a) The Board recently considered the permissibility, under section 4 of the

[6] It should be noted that in the event a third party should take exception to a Board order under section 2(g)(3) finding that control has been terminated, any rights such party might have would not be prejudiced by the order. If such party brought facts to the Board's attention indicating that control had not been terminated the Board would have ample authority to revoke its order and take necessary remedial action.

Orders issued under section 2(g)(3) are published in the Federal Reserve ''Bulletin.''

Bank Holding Company Act, of a subsidiary of a bank holding company acquiring and holding assets acquired in satisfaction of a debt previously contracted in good faith (a ''dpc'' acquisition). In the situation presented, a lending subsidiary of a bank holding company made a ''dpc'' acquisition of assets and transferred them to a wholly-owned subsidiary of the bank holding company for the purpose of effecting an orderly divestiture. The question presented was whether such ''dpc'' assets could be held indefinitely by a bank holding company subsidiary as incidental to its permissible lending activity.

(b) While the Board believes that ''dpc'' acquisitions may be regarded as normal, necessary and incidental to the business of lending, the Board does not believe that the holding of assets acquired ''dpc'' without any time restrictions is appropriate from the standpoint of prudent banking and in light of the prohibitions in section 4 of the Act against engaging in nonbank activities. If a nonbanking subsidiary of a bank holding company were permitted, either directly or through a subsidiary, to hold ''dpc'' assets of substantial amount over an extended period of time, the holding of such property could result in an unsafe or unsound banking practice or in the holding company engaging in an impermissible activity in connection with the assets, rather than liquidating them.

(c) The Board notes that section 4(c)(2) of the Bank Holding Company Act provides an exemption from the prohibitions of section 4 of the Act for bank holding company subsidiaries to acquire *shares* ''dpc''. It also provides that such ''dpc'' shares may be held for a period of two years, subject to the Board's authority to grant three one-year extensions up to a maximum of five years.[1] Viewed in light of the Congressional policy evidenced by section 4(c)(2), the Board believes that a lending subsidiary of a bank holding company or the holding company itself, should be permitted, as an incident to permissible lending activities, to make acquisitions of ''dpc'' *assets.* Consistent with the principles underlying the provisions of section 4(c)(2) of the Act and as a matter of prudent banking practice, such assets may be held for no longer than five years from the date of acquisition. Within the divestiture period it is expected that the company will make good faith efforts to dispose of ''dpc'' shares or assets at the earliest practicable date. While no specific authorization is necessary to hold such assets for the five-year period, after two years from the date of acquisition of such assets, the holding company should report annually on its efforts to accomplish divestiture to its Reserve Bank. The Reserve Bank will monitor the efforts of the company to effect an orderly divestiture, and may order divestiture before the end of the five-year period if supervisory concerns warrant such action.

(d) The Board recognizes that there are instances where a company may encounter particular difficulty in attempting to effect an orderly divestiture of ''dpc'' real estate holdings within the divestiture period, notwithstanding its persistent good faith efforts to dispose of such property. In the Depository Institutions Deregulation and Monetary Control Act of 1980, (Pub. L. 96–221) Congress, recognizing that real estate possesses unusual characteristics, amended the National Banking Act to permit national banks to hold real estate for five years and for an additional five-year period subject to certain conditions. Consistent with the policy underlying the recent Congressional enactment, and as a matter of supervisory policy, a bank holding company may be permitted to hold real estate acquired ''dpc'' beyond the initial five-year period provided that the value of the real estate on the books of the company has been written down to fair market value, the carrying costs are not significant in relation to the overall financial position of the company, and the company has made good faith efforts to effect divestiture. Companies holding real estate for this extended period are expected to make active efforts to dispose of it, and should keep the Reserve Bank advised

[1] The Board notes that where the dpc shares or other similar interests represent less than 5 percent of the total of such interests outstanding, they may be retained on the basis of section 4(c)(6), even if originally acquired dpc.

on a regular basis concerning their ongoing efforts. Fair market value should be derived from appraisals, comparable sales or some other reasonable method. In any case, ''dpc'' real estate would not be permitted to be held beyond 10 years from the date of its acquisition.

(e) With respect to the transfer by a subsidiary of other ''dpc'' shares or assets to another company in the holding company system, including a section 4(c)(1)(D) liquidating subsidiary, or to the holding company itself, such transfers would not alter the original divestiture period applicable to such shares or assets at the time of their acquisition. Moreover, to ensure that assets are not carried at inflated values for extended periods of time, the Board expects, in the case of all such intracompany transfers, that the shares or assets will be transferred at a value no greater than the fair market value at the time of transfer and that the transfer will be made in a normal arms-length transaction.

(f) With regard to ''dpc'' assets acquired by a banking subsidiary of a holding company, so long as the assets continue to be held by the bank itself, the Board will regard them as being solely within the regulatory authority of the primary supervisor of the bank.

(12 U.S.C. 1843 (c)(1)(d), (c)(2), (c)(8), and 1844 (b); 12 U.S.C. 1818)

[45 FR 49905, July 28, 1980]

§ 225.141 Operations subsidiaries of a bank holding company.

In orders approving the retention by a bank holding company of a 4(c)(8) subsidiary, the Board has stated that it would permit, without any specific regulatory approval, the formation of a wholly owned subsidiary of an approved 4(c)(8) company to engage in activities that such a company could itself engage in directly through a division or department. (*Northwestern Financial Corporation*, 65 Federal Reserve Bulletin 566 (1979).) Section 4(a)(2) of the Act provides generally that a bank holding company may engage directly in the business of managing and controlling banks and permissible nonbank activities, and in furnishing services directly to its subsidiaries. Even though section 4 of the Act generally prohibits the acquisition of shares of nonbanking organizations, the Board does not believe that such prohibition should apply to the formation by a holding company of a wholly-owned subsidiary to engage in activities that it could engage in directly. Accordingly, as a general matter, the Board will permit without any regulatory approval a bank holding company to form a wholly-owned subsidiary to perform servicing activities for subsidiaries that the holding company itself could perform directly or through a department or a division under section 4(a)(2) of the Act. The Board believes that permitting this type of subsidiary is not inconsistent with the nonbanking prohibitions of section 4 of the Act, and is consistent with the authority in section 4(c)(1)(C) of the Act, which permits a bank holding company, without regulatory approval, to form a subsidiary to perform services for its *banking* subsidiaries. The Board notes, however, that a servicing subsidiary established by a bank holding company in reliance on this interpretation will be an affiliate of the subsidiary bank of the holding company for the purposes of the lending restrictions of section 23A of the Federal Reserve Act. (12 U.S.C. 371c)

(12 U.S.C. 1843(a)(2) and 1844(b))

[45 FR 54326, July 15, 1980]

§ 225.142 Statement of policy concerning bank holding companies engaging in futures, forward and options contracts on U.S. Government and agency securities and money market instruments.

(a) *Purpose of financial contract positions.* In supervising the activities of bank holding companies, the Board has adopted and continues to follow the principle that bank holding companies should serve as a source of strength for their subsidiary banks. Accordingly, the Board believes that any positions that bank holding companies or their nonbank subsidiaries take in financial contracts should reduce risk exposure, that is, not be speculative.

(b) *Establishment of prudent written policies, appropriate limitations and internal controls and audit programs.* If the parent organization or nonbank subsidiary is taking or intends to take positions in financial contracts, that

company's board of directors should approve prudent written policies and establish appropriate limitations to insure that financial contract activities are performed in a safe and sound manner with levels of activity reasonably related to the organization's business needs and capacity to fulfill obligations. In addition, internal controls and internal audit programs to monitor such activity should be established. The board of directors, a duly authorized committee thereof or the internal auditors should review periodically (at least monthly) all financial contract positions to insure conformity with such policies and limits. In order to determine the company's exposure, all open positions should be reviewed and market values determined at least monthly, or more often, depending on volume and magnitude of positions.

(c) *Formulating policies and recording financial contracts.* In formulating its policies and procedures, the parent holding company may consider the interest rate exposure of its nonbank subsidiaries, but not that of its bank subsidiaries. As a matter of policy, the Board believes that any financial contracts executed to reduce the interest rate exposure of a bank affiliate of a holding company should be reflected on the books and records of the bank affiliate (to the extent required by the bank policy statements), rather than on the books and records of the parent company. If a bank has an interest rate exposure that management believes requires hedging with financial contracts, the bank should be the direct beneficiary of any effort to reduce that exposure. The Board also believes that final responsibility for financial contract transactions for the account of each affiliated bank should reside with the management of that bank.

(d) *Accounting.* The joint bank policy statements of March 12, 1980 include accounting guidelines for banks that engage in financial contract activities. Since the Financial Accounting Standards Board is presently considering accounting standards for contract activities, no specific accounting requirements for financial contracts entered into by parent bank holding companies and nonbank subsidiaries are being mandated at this time. The Board expects to review further developments in this area.

(e) *Board to monitor bank holding company transactions in financial contracts.* The Board intends to monitor closely bank holding company transactions in financial contracts to ensure that any such activity is consistent with maintaining a safe and sound banking system. In any cases where bank holding companies are found to be engaging in speculative practices, the Board is prepared to institute appropriate action under the Financial Institutions Supervisory Act of 1966, as amended.

(f) *Federal Reserve Bank notification.* Bank holding companies should furnish written notification to their District Federal Reserve Bank within 10 days after financial contract activities are begun by the parent or a nonbank subsidiary. Holding companies in which the parent or a nonbank subsidiary currently engage in financial contract activity should furnish notice by March 31, 1983.

(Secs. 5(b) and 8 of the Bank Holding Company Act (12 U.S.C. 1844 and 1847); sec. 8(b) of the Financial Institutions Supervisory Act (12 U.S.C. 1818(b))

[48 FR 7720, Feb. 24, 1983]

§ 225.143 Policy statement on nonvoting equity investments by bank holding companies.

(a) *Introduction.* (1) In recent months, a number of bank holding companies have made substantial equity investments in a bank or bank holding company (the ''acquiree'') located in states other than the home state of the investing company through acquisition of preferred stock or nonvoting common shares of the acquiree. Because of the evident interest in these types of investments and because they raise substantial questions under the Bank Holding Company Act (the ''Act''), the Board believes it is appropriate to provide guidance regarding the consistency of such arrangements with the Act.

(2) This statement sets out the Board's concerns with these investments, the considerations the Board will take into account in determining whether the investments are consistent with the Act, and the general scope of

arrangements to be avoided by bank holding companies. The Board recognizes that the complexity of legitimate business arrangements precludes rigid rules designed to cover all situations and that decisions regarding the existence or absence of control in any particular case must take into account the effect of the combination of provisions and covenants in the agreement as a whole and the particular facts and circumstances of each case. Nevertheless, the Board believes that the factors outlined in this statement provide a framework for guiding bank holding companies in complying with the requirements of the Act.

(b) *Statutory and regulatory provisions.* (1) Under section 3(a) of the Act, a bank holding company may not acquire direct or indirect ownership or control of more than 5 per cent of the voting shares of a bank without the Board's prior approval. (12 U.S.C. 1842(a)(3)). In addition, this section of the Act provides that a bank holding company may not, without the Board's prior approval, acquire control of a bank: That is, in the words of the statute, ''for any action to be taken that causes a bank to become a subsidiary of a bank holding company.'' (12 U.S.C. 1842(a)(2)). Under the Act, a bank is a subsidiary of a bank holding company if:

(i) The company directly or indirectly owns, controls, or holds with power to vote 25 per cent or more of the voting shares of the bank;

(ii) The company controls in any manner the election of a majority of the board of directors of the bank; or

(iii) The Board determines, after notice and opportunity for hearing, that the company has the power, directly or indirectly, to exercise a controlling influence over the management or policies of the bank. (12 U.S.C. 1841(d)).

(2) In intrastate situations, the Board may approve bank holding company acquisitions of additional banking subsidiaries. However, where the acquiree is located outside the home state of the investing bank holding company, section 3(d) of the Act prevents the Board from approving any application that will permit a bank holding company to ''acquire, directly or indirectly, any voting shares of, interest in, or all or substantially all of the assets of any additional bank.'' (12 U.S.C. 1842(d)(1)).

(c) *Review of agreements.* (1) In apparent expectation of statutory changes that might make interstate banking permissible, bank holding companies have sought to make substantial equity investments in other bank holding companies across state lines, but without obtaining more than 5 per cent of the voting shares or control of the acquiree. These investments involve a combination of the following arrangements:

(i) Options on, warrants for, or rights to convert nonvoting shares into substantial blocks of voting securities of the acquiree bank holding company or its subsidiary bank(s);

(ii) Merger or asset acquisition agreements with the out-of-state bank or bank holding company that are to be consummated in the event interstate banking is permitted;

(iii) Provisions that limit or restrict major policies, operations or decisions of the acquiree; and

(iv) Provisions that make acquisition of the acquiree or its subsidiary bank(s) by a third party either impossible or economically impracticable.

The various warrants, options, and rights are not exercisable by the investing bank holding company unless interstate banking is permitted, but may be transferred by the investor either immediately or after the passage of a period of time or upon the occurrence of certain events.

(2) After a careful review of a number of these agreements, the Board believes that investments in nonvoting stock, absent other arrangements, can be consistent with the Act. Some of the agreements reviewed appear consistent with the Act since they are limited to investments of relatively moderate size in nonvoting equity that may become voting equity only if interstate banking is authorized.

(3) However, other agreements reviewed by the Board raise substantial problems of consistency with the control provisions of the Act because the investors, uncertain whether or when interstate banking may be authorized, have evidently sought to assure the soundness of their investments, prevent takeovers by others, and allow for

sale of their options, warrants, or rights to a person of the investor's choice in the event a third party obtains control of the acquiree or the investor otherwise becomes dissatisfied with its investment. Since the Act precludes the investors from protecting their investments through ownership or use of voting shares or other exercise of control, the investors have substituted contractual agreements for rights normally achieved through voting shares.

(4) For example, various covenants in certain of the agreements seek to assure the continuing soundness of the investment by substantially limiting the discretion of the acquiree's management over major policies and decisions, including restrictions on entering into new banking activities without the investor's approval and requirements for extensive consultations with the investor on financial matters. By their terms, these covenants suggest control by the investing company over the management and policies of the acquiree.

(5) Similarly, certain of the agreements deprive the acquiree bank holding company, by covenant or because of an option, of the right to sell, transfer, or encumber a majority or all of the voting shares of its subsidiary bank(s) with the aim of maintaining the integrity of the investment and preventing takeovers by others. These long-term restrictions on voting shares fall within the presumption in the Board's Regulation Y that attributes control of shares to any company that enters into any agreement placing long-term restrictions on the rights of a holder of voting securities. (12 CFR 225.2(b)(4)).

(6) Finally, investors wish to reserve the right to sell their options, warrants or rights to a person of their choice to prevent being locked into what may become an unwanted investment. The Board has taken the position that the ability to control the ultimate disposition of voting shares to a person of the investor's choice and to secure the economic benefits therefrom indicates control of the shares under the Act.[1] Moreover, the ability to transfer rights to large blocks of voting shares, even if nonvoting in the hands of the investing company, may result in such a substantial position of leverage over the management of the acquiree as to involve a structure that inevitably results in control prohibited by the Act.

(d) *Provisions that avoid control.* (1) In the context of any particular agreement, provisions of the type described above may be acceptable if combined with other provisions that serve to preclude control. The Board believes that such agreements will not be consistent with the Act unless provisions are included that will preserve management's discretion over the policies and decisions of the acquiree and avoid control of voting shares.

(2) As a first step towards avoiding control, covenants in any agreement should leave management free to conduct banking and permissible nonbanking activities. Another step to avoid control is the right of the acquiree to ''call'' the equity investment and options or warrants to assure that covenants that may become inhibiting can be avoided by the acquiree. This right makes such investments or agreements more like a loan in which the borrower has a right to escape covenants and avoid the lender's influence by prepaying the loan.

(3) A measure to avoid problems of control arising through the investor's control over the ultimate disposition of rights to substantial amounts of voting shares of the acquiree would be a provision granting the acquiree a right of first refusal before warrants, options or other rights may be sold and requiring a public and dispersed distribution of these rights if the right of first refusal is not exercised.

(4) In this connection, the Board believes that agreements that involve rights to less than 25 percent of the voting shares, with a requirement for a dispersed public distribution in the event of sale, have a much greater prospect of achieving consistency with the Act than agreements involving a greater percentage. This guideline is drawn by analogy from the provision in the Act that ownership of 25 percent or more of the voting securities of a bank constitutes control of the bank.

[1] *See* Board letter dated March 18, 1982, to C. A. Cavendes, Sociedad Financiera.

(5) The Board expects that one effect of this guideline would be to hold down the size of the nonvoting equity investment by the investing company relative to the acquiree's total equity, thus avoiding the potential for control because the investor holds a very large proportion of the acquiree's total equity. Observance of the 25 percent guideline will also make provisions in agreements providing for a right of first refusal or a public and widely dispersed offering of rights to the acquiree's shares more practical and realistic.

(6) Finally, certain arrangements should clearly be avoided regardless of other provisions in the agreement that are designed to avoid control. These are:

(i) Agreements that enable the investing bank holding company (or its designee) to direct in any manner the voting of more than 5 per cent of the voting shares of the acquiree;

(ii) Agreements whereby the investing company has the right to direct the acquiree's use of the proceeds of an equity investment by the investing company to effect certain actions, such as the purchase and redemption of the acquiree's voting shares; and

(iii) The acquisition of more than 5 per cent of the voting shares of the acquiree that ''simultaneously'' with their acquisition by the investing company become nonvoting shares, remain nonvoting shares while held by the investor, and revert to voting shares when transferred to a third party.

(e) *Review by the Board.* This statement does not constitute the exclusive scope of the Board's concerns, nor are the considerations with respect to control outlined in this statement an exhaustive catalog of permissible or impermissible arrangements. The Board has instructed its staff to review agreements of the kind discussed in this statement and to bring to the Board's attention those that raise problems of consistency with the Act. In this regard, companies are requested to notify the Board of the terms of such proposed merger or asset acquisition agreements or nonvoting equity investments prior to their execution or consummation.

[47 FR 30966, July 16, 1982]

§ 225.145 Limitations established by the Competitive Equality Banking Act of 1987 on the activities and growth of nonbank banks.

(a) *Introduction.* Effective August 10, 1987, the Competitive Equality Banking Act of 1987 (''CEBA'') redefined the term ''bank'' in the Bank Holding Company Act (''BHC Act'' or ''Act'') to include any bank the deposits of which are insured by the Federal Deposit Insurance Corporation as well as any other institution that accepts demand or checkable deposit accounts and is engaged in the business of making commercial loans. 12 U.S.C. 1841(c). CEBA also contained a grandfather provision for certain companies affected by this redefinition. CEBA amended section 4 of the BHC Act to permit a company that on March 5, 1987, controlled a nonbank bank (an institution that became a bank as a result of enactment of CEBA) and that was not a bank holding company on August 9, 1987, to retain its nonbank bank and not be treated as a bank holding company for purposes of the BHC Act if the company and its subsidiary nonbank bank observe certain limitations imposed by CEBA.[1] Certain of these limitations are codified in section 4(f)(3) of the BHC Act and generally restrict nonbank banks from commencing new activities or certain cross-marketing activities with affiliates after March 5, 1987, or permitting overdrafts for affiliates or incurring overdrafts on behalf of affiliates at a Federal Reserve Bank. 12 U.S.C. 1843(f)(3).[2] The Board's views regarding

[1] 12 U.S.C. 1843(f). Such a company is treated as a bank holding company, however, for purposes of the anti-tying provisions in section 106 of the BHC Act Amendments of 1970 (12 U.S.C. 1971 *et seq.*) and the insider lending limitations of section 22(h) of the Federal Reserve Act (12 U.S.C. 375b). The company is also subject to certain examination and enforcement provisions to assure compliance with CEBA.

[2] CEBA also prohibits, with certain limited exceptions, a company controlling a grandfathered nonbank bank from acquiring control of an additional bank or thrift institution or acquiring, directly or indirectly after March 5, 1987, more than 5 percent of the assets or shares of a bank or thrift institution. 12 U.S.C. 1843(f)(2).

the meaning and scope of these limitations are set forth below and in provisions of the Board's Regulation Y (12 CFR 225.52).

(b) *Congressional findings.* (1) At the outset, the Board notes that the scope and application of the Act's limitations on nonbank banks must be guided by the Congressional findings set out in section 4(f)(3) of the BHC Act. Congress was aware that these nonbank banks had been acquired by companies that engage in a wide range of nonbanking activities, such as retailing and general securities activities that are forbidden to bank holding companies under section 4 of the BHC Act. In section 4(f)(3), Congress found that nonbank banks controlled by grandfathered nonbanking companies may, because of their relationships with affiliates, be involved in conflicts of interest, concentration of resources, or other effects adverse to bank safety and soundness. Congress also found that nonbank banks may be able to compete unfairly against banks controlled by bank holding companies by combining banking services with financial services not permissible for bank holding companies. Section 4(f)(3) states that the purpose of the nonbank bank limitations is to minimize any such potential adverse effects or inequities by restricting the activities of nonbank banks until further Congressional action in the area of bank powers could be undertaken. Similarly, the Senate Report accompanying CEBA states that the restrictions CEBA places on nonbank banks ''will help prevent existing nonbank banks from changing their basic character * * * while Congress considers proposals for comprehensive legislation; from drastically eroding the separation of banking and commerce; and from increasing the potential for unfair competition, conflicts of interest, undue concentration of resources, and other adverse effects.'' S. Rep. No. 100–19, 100th Cong., 1st Sess. 12 (1987). *See also* H. Rep. No. 100–261, 100th Cong., 1st Sess. 124 (1987) (the ''Conference Report'').

(2) Thus, Congress explicitly recognized in the statute itself that nonbanking companies controlling grandfathered nonbank banks, which include the many of the nation's largest commercial and financial organizations, were being accorded a significant competitive advantage that could not be matched by bank holding companies because of the general prohibition against nonbanking activities in section 4 of the BHC Act. Congress recognized that this inequality in regulatory approach could inflict serious competitive harm on regulated bank holding companies as the grandfathered entities sought to exploit potential synergies between banking and commercial products and services. *See* Conference Report at 125–126. The basic and stated purpose of the restrictions on grandfathered nonbank banks is to minimize these potential anticompetitive effects.

(3) The Board believes that the specific CEBA limitations should be implemented in light of these Congressional findings and the legislative intent reflected in the plain meaning of the terms used in the statute. In those instances when the language of the statute did not provide clear guidance, legislative materials and the Congressional intent manifested in the overall statutory structure were considered. The Board also notes that prior precedent requires that grandfather exceptions in the BHC Act, such as the nonbank bank limitations and particularly the exceptions thereto, are to be interpreted narrowly in order to ensure the proper implementation of Congressional intent.[3]

(c) *Activity limitation*—(1) *Scope of activity.* (i) The first limitation established under section 4(f)(3) provides that a nonbank bank shall not ''engage in any activity in which such bank was not lawfully engaged as of March 5, 1987.'' The term *activity* as used in this provision of CEBA is not defined. The structure and placement of the CEBA activity restriction within section 4 of the BHC Act and its legislative history do, however, provide direction as to certain transactions that Congress intended to treat as separate activities, thereby providing guidance as to the meaning Congress intended to ascribe

[3] *E.g., Maryland National Corporation,* 73 Federal Reserve Bulletin 310, 313–314 (1987). *Cf., Spokane & Inland Empire Railroad Co.* v. *United States,* 241 U.S. 344, 350 (1915).

to the term generally. First, it is clear that the term *activity* was not meant to refer to banking as a single activity. To the contrary, the term must be viewed as distinguishing between deposit taking and lending activities and treating demand deposit-taking as a separate activity from general deposit-taking and commercial lending as separate from the general lending category.

(ii) Under the activity limitation, a nonbank bank may engage only in activities in which it was ''lawfully engaged'' as of March 5, 1987. As of that date, a nonbank bank could not have been engaged in both demand deposit-taking and commercial lending activity without placing it and its parent holding company in violation of the BHC Act. Thus, under the activity limitations, a nonbank bank could not after March 5, 1987, commence the demand deposit-taking or commercial lending activity that it did not conduct as of March 5, 1987. The debates and Senate and Conference Reports on CEBA confirm that Congress intended the activity limitation to prevent a grandfathered nonbank bank from converting itself into a full-service bank by both offering demand deposits and engaging in the business of making commercial loans.[4] Thus, these types of transactions provide a clear guide as to the type of banking transactions that would constitute activities under CEBA and the degree of specificity intended by Congress in interpreting that term.

(iii) It is also clear that the activity limitation was not intended simply to prevent a nonbank bank from both accepting demand deposits and making commercial loans; it has a broader scope and purpose. If Congress had meant the term to refer to just these two activities, it would have used the restriction it used in another section of CEBA dealing with nonbank banks owned by bank holding companies which has this result, *i.e.*, the nonbank bank could not engage in any activity that would have caused it to become a bank under the prior bank definition in the Act. *See* 12 U.S.C. 1843(g)(1)(A). Indeed, an earlier version of CEBA under consideration by the Senate Banking Committee contained such a provision for nonbank banks owned by commercial holding companies, which was deleted in favor of the broader activity limitation actually enacted. Committee Print No. 1, (Feb. 17, 1987). In this regard, both the Senate Report and Conference Report refer to demand deposit-taking and commercial lending as examples of activities that could be affected by the activity limitation, not as the sole activities to be limited by the provision.[5]

(iv) Finally, additional guidance as to the meaning of the term *activity* is provided by the statutory context in which the term appears. The activity limitation is contained in section 4 of the BHC Act, which regulates the investments and activities of bank holding companies and their nonbank subsidiaries. The Board believes it reasonable to conclude that by placing the CEBA activity limitation in section 4 of the BHC Act, Congress meant that Board and judicial decisions regarding the meaning of the term *activity* in that section be looked to for guidance. This is particularly appropriate given the fact that grandfathered nonbank banks, whether owned by bank holding companies or unregulated holding companies, were treated as nonbank companies and not banks before enactment of CEBA.

(v) This interpretation of the term activity draws support from comments by Senator Proxmire during the Senate's consideration of the provision that the term was not intended to apply ''on a product-by-product, customer-by-customer basis.'' 133 Cong. Rec. S4054–5 (daily ed. March 27, 1987). This is the same manner in which the Board has interpreted the term activity in the nonbanking provision of section 4 as referring to generic categories

[4] Conference Report at 124–25; S. Rep. No. 100–19 at 12, 32; H. Rep. No. 99–175, 99th Cong., 1st Sess. 3 (1985) (''the activities limitation is to prevent an institution engaged in a limited range of functions from expanding into new areas and becoming, in essence, a full-service bank''); 133 Cong. Rec. S4054 (daily ed. March 27, 1987); (Comments of Senator Proxmire).

[5] Conference Report at 124–125; S. Rep. No. 100–19 at 32.

of activities, not to discrete products and services.

(vi) Accordingly, consistent with the terms and purposes of the legislation and the Congressional intent to minimize unfair competition and the other adverse effects set out in the CEBA findings, the Board concludes that the term *activity* as used in section 4(f)(3) means any line of banking or nonbanking business. This definition does not, however, envision a product-by-product approach to the activity limitation. The Board believes it would be helpful to describe the application of the activity limitation in the context of the following major categories of activities: deposit-taking, lending, trust, and other activities engaged in by banks.

(2) *Deposit-taking activities.* (i) With respect to deposit-taking, the Board believes that the activity limitation in section 4(f)(3) generally refers to three types of activity: demand deposit-taking; non-demand deposit-taking with a third party payment capability; and time and savings deposit-taking without third party payment powers. As previously discussed, it is clear from the terms and intent of CEBA that the activity limitation would prevent, and was designed to prevent, nonbank banks that prior to the enactment of CEBA had refrained from accepting demand deposits in order to avoid coverage as a *bank* under the BHC Act, from starting to take these deposits after enactment of CEBA and thus becoming full-service banks. Accordingly, CEBA requires that the taking of demand deposits be treated as a separate activity.

(ii) The Board also considers nondemand deposits withdrawable by check or other similar means for payment to third parties or others to constitute a separate line of business for purposes of applying the activity limitation. In this regard, the Board has previously recognized that this line of businesss constitutes a permissible but separate activity under section 4 of the BHC Act. Furthermore, the offering of accounts with transaction capability requires different expertise and systems than non-transaction deposit-taking and represented a distinct new activity that traditionally separated banks from thrift and similar institutions.

(iii) Support for this view may also be found in the House Banking Committee report on proposed legislation prior to CEBA that contained a similar prohibition on new activities for nonbank banks. In discussing the activity limitation, the report recognized a distinction between demand deposits and accounts with transaction capability and those without transaction capability:

> With respect to deposits, the Committee recognizes that it is legitimate for an institution currently involved in offering demand deposits or other third party transaction accounts to make use of new technologies that are in the process of replacing the existing check-based, paper payment system. Again, however, the Committee does not believe that technology should be used as a lever for an institution that was only incidentally involved in the payment system to transform itself into a significant offeror of transaction account capability.[6]

(iv) Finally, this distinction between demand and nondemand checkable accounts and accounts not subject to withdrawal by check was specifically recognized by Congress in the redefinition of the term *bank* in CEBA to include an institution that takes demand deposits or ''deposits that the depositor may withdraw by check or other means for payment to third parties or others'' as well as in various exemptions from that definition for trust companies, credit card banks, and certain industrial banks.[7]

(v) Thus, an institution that as of March 5, 1987, offered only time and savings accounts that were not withdrawable by check for payment to third parties could not thereafter begin offering accounts with transaction capability, for example, NOW accounts or other types of transaction accounts.

(3) *Lending.* As noted, the CEBA activity limitation does not treat lending as a single activity; it clearly distinguishes between commercial and other types of lending. This distinction is also reflected in the definition of *bank* in the BHC Act in effect both prior to

[6] H. Rep. No. 99–175, 99th Cong., 1st Sess. 13 (1985).

[7] See 12 U.S.C. 1841(c)(2) (D), (F), (H), and (I).

and after enactment of CEBA as well as in various of the exceptions from this definition. In addition, commercial lending is a specialized form of lending involving different techniques and analysis from other types of lending. Based upon these factors, the Board would view commercial lending as a separate and distinct activity for purposes of the activity limitation in section 4(f)(3). The Board's decisions under section 4 of the BHC Act have not generally differentiated between types of commercial lending, and thus the Board would view commercial lending as a single activity for purposes of CEBA. Thus, a nonbank bank that made commercial loans as of March 5, 1987, could make any type of commercial loan thereafter.

(i) *Commercial lending.* For purposes of the activity limitation, a commercial loan is defined in accordance with the Supreme Court's decision in *Board of Governors* v. *Dimension Financial Corporation,* 474 U.S. 361 (1986), as a direct loan to a business customer for the purpose of providing funds for that customer's business. In this regard, the Board notes that whether a particular transaction is a commercial loan must be determined not from the face of the instrument, but from the application of the definition of commercial loan in the *Dimension* decision to that transaction. Thus, certain transactions of the type mentioned in the Board's ruling at issue in *Dimension* and in the Senate and Conference Reports in the CEBA legislation[8] would be commercial loans if they meet the test for commercial loans established in *Dimension*. Under this test, a commercial loan would not include, for example, an open-market investment in a commercial entity that does not involve a borrower-lender relationship or negotiation of credit terms, such as a money market transaction.

(ii) *Other lending.* Based upon the guidance in the Act as to the degree of specificity required in applying the activity limitation with respect to lending, the Board believes that, in addition to commercial lending, there are three other types of lending activities: consumer mortgage lending, consumer credit card lending, and other consumer lending. Mortgage lending and credit card lending are recognized, discrete lines of banking and business activity, involving techniques and processes that are different from and more specialized than those required for general consumer lending. For example, these activities are, in many cases, conducted by specialized institutions, such as mortgage companies and credit card institutions, or through separate organizational structures within an institution, particularly in the case of mortgage lending. Additionally, the Board's decisions under section 4 of the Act have recognized mortgage banking and credit card lending as separate activities for bank holding companies. The Board's Regulation Y reflects this specialization, noting as examples of permissible lending activity: consumer finance, credit card and mortgage lending. 12 CFR 225.25(b)(1). Finally, CEBA itself recognizes the specialized nature of credit card lending by exempting an institution specializing in that activity from the bank definition. For purpose of the activity limitation, a consumer mortgage loan will mean any loan to an individual that is secured by real estate and that is not a commercial loan. A credit card loan would be any loan made to an individual by means of a credit card that is not a commercial loan.

(4) *Trust activities.* Under section 4 of the Act, the Board has historically treated trust activities as a single activity and has not differentiated the function on the basis of whether the customer was an individual or a business. *See* 12 CFR 225.25(b)(3). Similarly, the trust company exemption from the bank definition in CEBA makes no distinction between various types of trust activities. Accordingly, the Board would view trust activities as a separate activity without additional differentiation for purposes of the activity limitation in section 4(f)(3).

(5) *Other activities.* With respect to activities other than the various traditional deposit-taking, lending or trust activities, the Board believes it appropriate, for the reasons discussed above,

[8] S. Rep. No. 100–19 at 31; Conference Report at 123.

to apply the activity limitation in section 4(f)(3) as the term *activity* generally applies in other provisions of section 4 of the BHC Act. Thus, a grandfathered nonbank bank could not, for example, commence after March 5, 1987, any of the following activities (unless it was engaged in such an activity as of that date): discount securities brokerage, full-service securities brokerage investment advisory services, underwriting or dealing in government securities as permissible for member banks, foreign exchange transaction services, real or personal property leasing, courier services, data processing for third parties, insurance agency activities,[9] real estate development, real estate brokerage, real estate syndication, insurance underwriting, management consulting, futures commission merchant, or activities of the general type listed in §225.25(b) of Regulation Y.

(6) *Meaning of engaged in.* In order to be *engaged in* an activity, a nonbank bank must demonstrate that it had a program in place to provide a particular product or service included within the grandfathered activity to a customer and that it was in fact offering the product or service to customers as of March 5, 1987. Thus, a nonbank bank is not engaged in an activity as of March 5, 1987, if the product or service in question was in a planning state as of that date and had not been offered or delivered to a customer. Consistent with prior Board interpretations of the term activity in the grandfather provisions of section 4, the Board does not believe that a company may be engaged in an activity on the basis of a single isolated transaction that was not part of a program to offer the particular product or to conduct in the activity on an ongoing basis. For example, a nonbank bank that held an interest in a single real estate project would not thereby be engaged in real estate development for purposes of this provision, unless evidence was presented indicating the interest was held under a program to commence a real estate development business.

(7) *Meaning of as of* The Board believes that the grandfather date ''as of March 5, 1987'' as used throughout section 4(f)(3) should refer to activities engaged in on March 5, 1987, or a reasonably short period preceding this date not exceeding 13 months. 133 Cong. Rec. S3957 (daily ed. March 26, 1987). (Remarks of Senators Dodd and Proxmire). Activities that the institution had terminated prior to March 5, 1988, however, would not be considered to have been conducted or engaged in *as of* March 5. For example, if within 13 months of March 5, 1987, the nonbank bank had terminated its commercial lending activity in order to avoid the *bank* definition in the Act, the nonbank bank could not recommence that activity after enactment of CEBA.

(d) *Cross-marketing limitation*—(1) *In general.* Section 4(f)(3) also limits cross-marketing activities by nonbank banks and their affiliates. Under this provision, a nonbank bank may not offer or market a product or service of an affiliate unless the product or service may be offered by bank holding companies generally under section 4(c)(8) of the BHC Act. In addition, a nonbank bank may not permit any of its products or services to be offered or marketed by or through a nonbank affiliate unless the affiliate engages only in activities permissible for a bank holding company under section 4(c)(8). These limitations are subject to an exception for products or services that were being so offered or marketed as of March 5, 1987, but only in the same manner in which they were being offered or marketed as of that date.

(2) *Examples of impermissible cross-marketing.* The Conference Report illustrates the application of this limitation to the following two covered transactions: (i) products and services of an affiliate that bank holding companies may not offer under the BHC Act, and (ii) products and services of the nonbank bank. In the first case, the restrictions would prohibit, for example, a company from marketing life insurance or automotive supplies through its affiliate nonbank bank because these products are not generally

[9] In this area, section 4 of the Act does not treat all insurance agency activities as a single activity. Thus, for example, the Act treats the sale of credit-related life, accident and health insurance as a separate activity from general insurance agency activities. See 12 U.S.C. 1843(c)(8).

permissible under the BHC Act. Conference Report at 126. In the second case, a nonbank bank may not permit its products or services to be offered or marketed through a life insurance affiliate or automobile parts retailer because these affiliates engage in activities prohibited under the BHC Act. *Id.*

(3) *Permissible cross-marketing.* On the other hand, a nonbank bank could offer to its customers consumer loans from an affiliated mortgage banking or consumer finance company. These affiliates could likewise offer their customers the nonbank bank's products or services provided the affiliates engaged only in activities permitted for bank holding companies under the closely-related-to-banking standard of section 4(c)(8) of the BHC Act. If the affiliate is engaged in both permissible and impermissible activities within the meaning of section 4(c)(8) of the BHC Act, however, the affiliate could not offer or market the nonbank bank's products or services.

(4) *Product approach to cross-marketing restriction.* (i) Unlike the activity restrictions, the cross-marketing restrictions of CEBA apply by their terms to individual products and services. Thus, an affiliate of a nonbank bank that was engaged in activities that are not permissible for bank holding companies and that was marketing a particular product or service of a nonbank bank on the grandfather date could continue to market that product and, as discussed below, could change the terms and conditions of the loan. The nonbank affiliate could not, however, begin to offer or market another product or service of the nonbank bank.

(ii) The Board believes that the term *product or service* must be interpreted in light of its accepted ordinary commercial usage. In some instances, commercial usage has identified a group of products so closely related that they constitute a product line (*e.g.,* certificates of deposit) and differences in versions of the product (*e.g.,* a one-year certificate of deposit) simply represent a difference in the terms of the product.[10] This approach is consistent with the treatment in CEBA's legislative history of certificates of deposit as a product line rather than each particular type of CD as a separate product.[11]

(iii) In the area of consumer lending, the Board believes the following provide examples of different consumer loan products: mortgage loans to finance the purchase of the borrower's residence, unsecured consumer loans, consumer installment loans secured by the personal property to be purchased (*e.g.* automobile, boat or home appliance loans), or second mortgage loans.[12] Under this interpretation, a nonbank bank that offered automobile loans through a nonbank affiliate on the grandfather date could market boat loans, appliance loans or any type of secured consumer installment loan through that affiliate. It could not, however, market unsecured consumer loans, home mortgage loans or other types of consumer loans.

(iv) In other areas, the Board believes that the determination as to what constitutes a product or service should be made on a case-by-case basis consistent with the principles that the terms *product or service* must be interpreted in accordance with their ordinary commercial usage and must be narrower in scope than the definition of activity. Essentially, the concept applied in this analysis is one of permitting the continuation of the specific product marketing activity that was undertaken as

[10] American Bankers Association, *Banking Terminology* (1981).

[11] During the Senate debates on CEBA, Senator Proxmire in response to a statement from Senator Cranston that the joint-marketing restrictions do not lock into place the specific terms or conditions of the particular grandfathered product or service, stated:

That is correct. For example, if a nonbank bank was jointly marketing on March 5, 1987, a 3 year, $5,000 certificate of deposit, this bill would not prohibit offering in the same manner a 1 year, $2,000 certificate of deposit with a different interest rate. 133 Cong. Rec. S3959 (daily ed. March 26, 1987).

[12] In this regard, the Supreme Court in *United States* v. *Philadelphia National Bank,* noted that ''the principal banking products are of course various types of credit, for example: unsecured personal and business loans, mortgage loans, loans secured by securities or accounts receivable, automobile installment and consumer goods, installment loans, tuition financing, bank credit cards, revolving credit funds.'' 374 U.S. 321, 326 n.5 (1963).

of March 5, 1987. Thus, for example, while insurance underwriting may constitute a separate activity under CEBA, a nonbank bank could not market a life insurance policy issued by the affiliate if on the grandfather date it had only marketed homeowners' policies issued by the affiliate.

(5) *Change in terms and conditions permitted.* (i) The cross-marketing restrictions would not limit the ability of the institution to change the specific terms and conditions of a particular grandfathered product or service. The Conference Report indicates a legislative intent not to lock into place the specific terms or conditions of a grandfathered product or service. Conference Report at 126. For example, a nonbank bank marketing a three-year, $5,000 certificate of deposit through an affiliate under the exemption could offer a one-year $2,000 certificate of deposit with a different interest rate after the grandfather date. *See* footnote 11 above. Modifications that alter the type of product, however, are not permitted. Thus, a nonbank bank that marketed through affiliates on March 5, 1987, only certificates of deposit could not commence marketing MMDA's or NOW accounts after the grandfather date.

(ii) General changes in the character of the product or service as the result of market or technological innovation are similarly permitted to the extent that they do not transform a grandfathered product into a new product. Thus, an unsecured line of credit could not be modified to include a lien on the borrower's residence without becoming a new product.

(6) *Meaning of offer or market.* In the Board's opinion, the terms *offer or market* in the cross-marketing restrictions refer to the presentation to a customer of an institution's products or service through any type of program, including telemarketing, advertising brochures, direct mailing, personal solicitation, customer referrals, or joint-marketing agreements or presentations. An institution must have offered or actually marketed the product or service on March 5 or shortly before that date (as discussed above) to qualify for the grandfather privilege. Thus, if the cross-marketing program was in the planning stage on March 5, 1987, the program would not quality for grandfather treatment under CEBA.

(7) *Limitations on cross-marketing to in the same manner.* (i) The cross-marketing restriction in section 4(f)(3) contains a grandfather provision that permits products or services that would otherwise be prohibited from being offered or marketed under the provision to continue to be offered or marketed by a particular entity if the products or services were being so offered or marketed as of March 5, 1987, but ''only in the same manner in which they were being offered or marketed as of that date.'' Thus, to qualify for the grandfather provision, the manner of offering or marketing the otherwise prohibited product or service must remain the same as on the grandfather date.

(ii) In interpreting this provision, the Board notes that Congress designed the joint-marketing restrictions to prevent the significant risk to the public posed by the conduct of such activities by insured banks affiliated with companies engaged in general commerce, to ensure objectivity in the credit-granting process and to ''minimize the unfair competitive advantage that grandfathered commercial companies owning nonbank banks might otherwise engage over regulated bank holding companies and our competing commercial companies that have no subsidiary bank.'' Conference Report at 125–126. The Board believes that determinations regarding the manner of cross-marketing of a particular product or service may best be accomplished by applying the limitation to the particular facts in each case consistent with the stated purpose of this provision of CEBA and the general principle that grandfather restrictions and exceptions to general prohibitions must be narrowly construed in order to prevent the exception from nullifying the rule. Essentially, as in the scope of the term ''product or service'', the guiding principle of Congressional intent with respect to this term is to permit only the continuation of the specific types of cross-marketing activity that were undertaken as of March 5, 1987.

(8) *Eligibility for cross-marketing grandfather exemption.* The Conference Report also clarifies that entitlement to

an exemption to continue to cross-market products and services otherwise prohibited by the statute applies only to the specific company that was engaged in the activity as of March 5, 1987. Conference Report at 126. Thus, an affiliate that was not engaged in cross-marketing products or services as of the grandfather date may not commence these activities under the exemption even if such activities were being conducted by another affiliate. *Id.*; *see also* S. Rep. No. 100–19 at 33–34.

(e) *Eligibility for grandfathered nonbank bank status.* In reviewing the reports required by CEBA, the Board notes that a number of institutions that had not commenced business operations on August 10, 1987, the date of enactment of CEBA, claimed grandfather privileges under section 4(f)(3) of CEBA. To qualify for grandfather privileges under section 4(f)(3), the institution must have ''bec[o]me a bank as a result of the enactment of [CEBA]'' and must have been controlled by a nonbanking company on March 5, 1987. 12 U.S.C. 1843(f)(1)(A). An institution that did not have FDIC insurance on August 10, 1987, and that did not accept demand deposits or transaction accounts or engage in the business of commercial lending on that date, would not have become a *bank* as a result of enactment of CEBA. Thus, institutions that had not commenced operations on August 10, 1987, could not qualify for grandfather privileges under section 4(f)(3) of CEBA. This view is supported by the activity limitations of section 4(f)(3), which, as noted, limit the activities of grandfathered nonbank banks to those in which they were lawfully engaged as of March 5, 1987. A nonbank bank that had not commenced conducting business activities on March 5, 1987, could not after enactment of CEBA engage in any activities under this provision.

[Reg. Y, 53 FR 37746, Sept. 28, 1988, as amended by Reg. Y, 62 FR 9343, Feb. 28, 1997]

Subpart J—Merchant Banking Investments

SOURCE: Reg. Y, 66 FR 8484, Jan. 31, 2001, unless otherwise noted.

§ 225.170 What type of investments are permitted by this subpart, and under what conditions may they be made?

(a) *What types of investments are permitted by this subpart?* Section 4(k)(4)(H) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(H)) and this subpart authorize a financial holding company, directly or indirectly and as principal or on behalf of one or more persons, to acquire or control any amount of shares, assets or ownership interests of a company or other entity that is engaged in any activity not otherwise authorized for the financial holding company under section 4 of the Bank Holding Company Act. For purposes of this subpart, shares, assets or ownership interests acquired or controlled under section 4(k)(4)(H) and this subpart are referred to as ''merchant banking investments.'' A financial holding company may not directly or indirectly acquire or control any merchant banking investment except in compliance with the requirements of this subpart.

(b) *Must the investment be a bona fide merchant banking investment?* The acquisition or control of shares, assets or ownership interests under this subpart is not permitted unless it is part of a bona fide underwriting or merchant or investment banking activity.

(c) *What types of ownership interests may be acquired?* Shares, assets or ownership interests of a company or other entity include any debt or equity security, warrant, option, partnership interest, trust certificate or other instrument representing an ownership interest in the company or entity, whether voting or nonvoting.

(d) *Where in a financial holding company may merchant banking investments be made?* A financial holding company and any subsidiary (other than a depository institution or subsidiary of a depository institution) may acquire or control merchant banking investments. A financial holding company and its subsidiaries may not acquire or control merchant banking investments on behalf of a depository institution or subsidiary of a depository institution.

(e) *May assets other than shares be held directly?* A financial holding company may not under this subpart acquire or

control assets, other than debt or equity securities or other ownership interests in a company, unless:

(1) The assets are held by or promptly transferred to a portfolio company;

(2) The portfolio company maintains policies, books and records, accounts, and other indicia of corporate, partnership or limited liability organization and operation that are separate from the financial holding company and limit the legal liability of the financial holding company for obligations of the portfolio company; and

(3) The portfolio company has management that is separate from the financial holding company to the extent required by § 225.171.

(f) *What type of affiliate is required for a financial holding company to make merchant banking investments?* A financial holding company may not acquire or control merchant banking investments under this subpart unless the financial holding company qualifies under at least one of the following paragraphs:

(1) *Securities affiliate.* The financial holding company is or has an affiliate that is registered under the Securities Exchange Act of 1934 (15 U.S.C. 78c, 78o, 78o–4) as:

(i) A broker or dealer; or

(ii) A municipal securities dealer, including a separately identifiable department or division of a bank that is registered as a municipal securities dealer.

(2) *Insurance affiliate with an investment adviser affiliate.* The financial holding company controls:

(i) An insurance company that is predominantly engaged in underwriting life, accident and health, or property and casualty insurance (other than credit-related insurance), or providing and issuing annuities; and

(ii) A company that:

(A) Is registered with the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940 (15 U.S.C. 80b–1 *et seq.*); and

(B) Provides investment advice to an insurance company.

§ 225.171 What are the limitations on managing or operating a portfolio company held as a merchant banking investment?

(a) *May a financial holding company routinely manage or operate a portfolio company?* Except as permitted in paragraph (e) of this section, a financial holding company may not routinely manage or operate any portfolio company.

(b) *When does a financial holding company routinely manage or operate a company?*

(1) *Examples of routine management or operation*—(i) *Executive officer interlocks at the portfolio company.* A financial holding company routinely manages or operates a portfolio company if any director, officer or employee of the financial holding company serves as or has the responsibilities of an executive officer of the portfolio company.

(ii) Interlocks by executive officers of the financial holding company. (A) *Prohibition.* A financial holding company routinely manages or operates a portfolio company if any executive officer of the financial holding company serves as or has the responsibilities of an officer or employee of the portfolio company.

(B) *Definition.* For purposes of paragraph (b)(1)(ii)(A) of this section, the term ''financial holding company'' includes the financial holding company and only the following subsidiaries of the financial holding company:

(*1*) A securities broker or dealer registered under the Securities Exchange Act of 1934;

(*2*) A depository institution;

(*3*) An affiliate that engages in merchant banking activities under this subpart or insurance company investment activities under section 4(k)(4)(I) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(I));

(*4*) A small business investment company (as defined in section 302(b) of the Small Business Investment Act of 1958 (15 U.S.C. 682(b)) controlled by the financial holding company or by any depository institution controlled by the financial holding company; and

(5) Any other affiliate that engages in significant equity investment activities that are subject to a special capital charge under the capital adequacy rules or guidelines of the Board.

(iii) *Covenants regarding ordinary course of business.* A financial holding company routinely manages or operates a portfolio company if any covenant or other contractual arrangement exists between the financial holding company and the portfolio company that would restrict the portfolio company's ability to make routine business decisions, such as entering into transactions in the ordinary course of business or hiring officers or employees other than executive officers.

(2) *Presumptions of routine management or operation.* A financial holding company is presumed to routinely manage or operate a portfolio company if:

(i) Any director, officer, or employee of the financial holding company serves as or has the responsibilities of an officer (other than an executive officer) or employee of the portfolio company; or

(ii) Any officer or employee of the portfolio company is supervised by any director, officer, or employee of the financial holding company (other than in that individual's capacity as a director of the portfolio company).

(c) *How may a financial holding company rebut a presumption that it is routinely managing or operating a portfolio company?* A financial holding company may rebut a presumption that it is routinely managing or operating a portfolio company under paragraph (b)(2) of this section by presenting information to the Board demonstrating to the Board's satisfaction that the financial holding company is not routinely managing or operating the portfolio company.

(d) *What arrangements do not involve routinely managing or operating a portfolio company?*—(1) *Director representation at portfolio companies.* A financial holding company may select any or all of the directors of a portfolio company or have one or more of its directors, officers, or employees serve as directors of a portfolio company if:

(i) The portfolio company employs officers and employees responsible for routinely managing and operating the company; and

(ii) The financial holding company does not routinely manage or operate the portfolio company, except as permitted in paragraph (e) of this section.

(2) *Covenants or other provisions regarding extraordinary events.* A financial holding company may, by virtue of covenants or other written agreements with a portfolio company, restrict the ability of the portfolio company, or require the portfolio company to consult with or obtain the approval of the financial holding company, to take actions outside of the ordinary course of the business of the portfolio company. Examples of the types of actions that may be subject to these types of covenants or agreements include, but are not limited to, the following:

(i) The acquisition of significant assets or control of another company by the portfolio company or any of its subsidiaries;

(ii) Removal or selection of an independent accountant or auditor or investment banker by the portfolio company;

(iii) Significant changes to the business plan or accounting methods or policies of the portfolio company;

(iv) Removal or replacement of any or all of the executive officers of the portfolio company;

(v) The redemption, authorization or issuance of any equity or debt securities (including options, warrants or convertible shares) of the portfolio company or any borrowing by the portfolio company outside of the ordinary course of business;

(vi) The amendment of the articles of incorporation or by-laws (or similar governing documents) of the portfolio company; and

(vii) The sale, merger, consolidation, spin-off, recapitalization, liquidation, dissolution or sale of substantially all of the assets of the portfolio company or any of its significant subsidiaries.

(3) *Providing advisory and underwriting services to, and having consultations with, a portfolio company.* A financial holding company may:

(i) Provide financial, investment and management consulting advice to a

portfolio company in a manner consistent with and subject to any restrictions on such activities contained in §§ 225.28(b)(6) or 225.86(b)(1) of this part (12 CFR 225.28(b)(6) and 225.86(b)(1));

(ii) Provide assistance to a portfolio company in connection with the underwriting or private placement of its securities, including acting as the underwriter or placement agent for such securities; and

(iii) Meet with the officers or employees of a portfolio company to monitor or provide advice with respect to the portfolio company's performance or activities.

(e) *When may a financial holding company routinely manage or operate a portfolio company?*—(1) *Special circumstances required.* A financial holding company may routinely manage or operate a portfolio company only when intervention by the financial holding company is necessary or required to obtain a reasonable return on the financial holding company's investment in the portfolio company upon resale or other disposition of the investment, such as to avoid or address a significant operating loss or in connection with a loss of senior management at the portfolio company.

(2) *Duration Limited.* A financial holding company may routinely manage or operate a portfolio company only for the period of time as may be necessary to address the cause of the financial holding company's involvement, to obtain suitable alternative management arrangements, to dispose of the investment, or to otherwise obtain a reasonable return upon the resale or disposition of the investment.

(3) *Notice required for extended involvement.* A financial holding company may not routinely manage or operate a portfolio company for a period greater than nine months without prior written notice to the Board.

(4) *Documentation required.* A financial holding company must maintain and make available to the Board upon request a written record describing its involvement in routinely managing or operating a portfolio company.

(f) *May a depository institution or its subsidiary routinely manage or operate a portfolio company?*—(1) *In general.* A depository institution and a subsidiary of a depository institution may not routinely manage or operate a portfolio company in which an affiliated company owns or controls an interest under this subpart.

(2) *Definition applying provisions governing routine management or operation.* For purposes of this section other than paragraph (e) and for purposes of § 225.173(d), a financial holding company includes a depository institution controlled by the financial holding company and a subsidiary of such a depository institution.

(3) *Exception for certain subsidiaries of depository institutions.* For purposes of paragraph (e) of this section, a financial holding company includes a financial subsidiary held in accordance with section 5136A of the Revised Statutes (12 U.S.C. 24a) or section 46 of the Federal Deposit Insurance Act (12 U.S.C. 1831w), and a subsidiary that is a small business investment company and that is held in accordance with the Small Business Investment Act (15 U.S.C. 661 *et seq.*), and such a subsidiary may, in accordance with the limitations set forth in this section, routinely manage or operate a portfolio company in which an affiliated company owns or controls an interest under this subpart.

§ 225.172 What are the holding periods permitted for merchant banking investments?

(a) *Must investments be made for resale?* A financial holding company may own or control shares, assets and ownership interests pursuant to this subpart only for a period of time to enable the sale or disposition thereof on a reasonable basis consistent with the financial viability of the financial holding company's merchant banking investment activities.

(b) *What period of time is generally permitted for holding merchant banking investments?*—(1) *In general.* Except as provided in this section or § 225.173, a financial holding company may not, directly or indirectly, own, control or hold any share, asset or ownership interest pursuant to this subpart for a period that exceeds 10 years.

(2) *Ownership interests acquired from or transferred to companies held under this subpart.* For purposes of paragraph

(b)(1) of this section, shares, assets or ownership interests—

(i) Acquired by a financial holding company from a company in which the financial holding company held an interest under this subpart will be considered to have been acquired by the financial holding company on the date that the share, asset or ownership interest was acquired by the company; and

(ii) Acquired by a company from a financial holding company will be considered to have been acquired by the company on the date that the share, asset or ownership interest was acquired by the financial holding company if—

(A) The financial holding company held the share, asset, or ownership interest under this subpart; and

(B) The financial holding company holds an interest in the acquiring company under this subpart.

(3) *Interests previously held by a financial holding company under limited authority.* For purposes of paragraph (b)(1) of this section, any shares, assets, or ownership interests previously owned or controlled, directly or indirectly, by a financial holding company under any other provision of the Federal banking laws that imposes a limited holding period will if acquired under this subpart be considered to have been acquired by the financial holding company under this subpart on the date the financial holding company first acquired ownership or control of the shares, assets or ownership interests under such other provision of law. For purposes of this paragraph (b)(3), a financial holding company includes a depository institution controlled by the financial holding company and any subsidiary of such a depository institution.

(4) *Approval required to hold interests held in excess of time limit.* A financial holding company may seek Board approval to own, control or hold shares, assets or ownership interests of a company under this subpart for a period that exceeds the period specified in paragraph (b)(1) of this section. A request for approval must:

(i) Be submitted to the Board at least 90 days prior to the expiration of the applicable time period;

(ii) Provide the reasons for the request, including information that addresses the factors in paragraph (b)(5) of this section; and

(iii) Explain the financial holding company's plan for divesting the shares, assets or ownership interests.

(5) *Factors governing Board determinations.* In reviewing any proposal under paragraph (b)(4) of this section, the Board may consider all the facts and circumstances related to the investment, including:

(i) The cost to the financial holding company of disposing of the investment within the applicable period;

(ii) The total exposure of the financial holding company to the company and the risks that disposing of the investment may pose to the financial holding company;

(iii) Market conditions;

(iv) The nature of the portfolio company's business;

(v) The extent and history of involvement by the financial holding company in the management and operations of the company; and

(vi) The average holding period of the financial holding company's merchant banking investments.

(6) *Restrictions applicable to investments held beyond time period.* A financial holding company that directly or indirectly owns, controls or holds any share, asset or ownership interest of a company under this subpart for a total period that exceeds the period specified in paragraph (b)(1) of this section must—

(i) For purposes of determining the financial holding company's regulatory capital, apply to the financial holding company's adjusted carrying value of such shares, assets, or ownership interests a capital charge determined by the Board that must be:

(A) Higher than the maximum marginal Tier 1 capital charge applicable under the Board's capital adequacy rules or guidelines (*see* 12 CFR 225 Appendix A) to merchant banking investments held by that financial holding company; and

(B) In no event less than 25 percent of the adjusted carrying value of the investment; and

(ii) Abide by any other restrictions that the Board may impose in connection with granting approval under paragraph (b)(4) of this section.

§ 225.173 How are investments in private equity funds treated under this subpart?

(a) *What is a private equity fund?* For purposes of this subpart, a ''private equity fund'' is any company that:

(1) Is formed for the purpose of and is engaged exclusively in the business of investing in shares, assets, and ownership interests of financial and nonfinancial companies for resale or other disposition;

(2) Is not an operating company;

(3) No more than 25 percent of the total equity of which is held, owned or controlled, directly or indirectly, by the financial holding company and its directors, officers, employees and principal shareholders;

(4) Has a maximum term of not more than 15 years; and

(5) Is not formed or operated for the purpose of making investments inconsistent with the authority granted under section 4(k)(4)(H) of the Bank Holding Company Act (12 U.S.C. 1843(k)(4)(H)) or evading the limitations governing merchant banking investments contained in this subpart.

(b) *What form may a private equity fund take?* A private equity fund may be a corporation, partnership, limited liability company or other type of company that issues ownership interests in any form.

(c) *What is the holding period permitted for interests in private equity funds?*—(1) *In general.* A financial holding company may own, control or hold any interest in a private equity fund under this subpart and any interest in a portfolio company that is owned or controlled by a private equity fund in which the financial holding company owns or controls any interest under this subpart for the duration of the fund, up to a maximum of 15 years.

(2) *Request to hold interest for longer period.* A financial holding company may seek Board approval to own, control or hold an interest in or held through a private equity fund for a period longer than the duration of the fund in accordance with § 225.172(b) of this subpart.

(3) *Application of rules.* The rules described in § 225.172(b)(2) and (3) governing holding periods of interests acquired, transferred or previously held by a financial holding company apply to interests in, held through, or acquired from a private equity fund.

(d) *How do the restrictions on routine management and operation apply to private equity funds and investments held through a private equity fund?*—(1) *Portfolio companies held through a private equity fund.* A financial holding company may not routinely manage or operate a portfolio company that is owned or controlled by a private equity fund in which the financial holding company owns or controls any interest under this subpart, except as permitted under § 225.171(e).

(2) *Private equity funds controlled by a financial holding company.* A private equity fund that is controlled by a financial holding company may not routinely manage or operate a portfolio company, except as permitted under § 225.171(e).

(3) *Private equity funds that are not controlled by a financial holding company.* A private equity fund may routinely manage or operate a portfolio company so long as no financial holding company controls the private equity fund or as permitted under § 225.171(e).

(4) *When does a financial holding company control a private equity fund?* A financial holding company controls a private equity fund for purposes of this subpart if the financial holding company, including any director, officer, employee or principal shareholder of the financial holding company:

(i) Serves as a general partner, managing member, or trustee of the private equity fund (or serves in a similar role with respect to the private equity fund);

(ii) Owns or controls 25 percent or more of any class of voting shares or similar interests in the private equity fund;

(iii) In any manner selects, controls or constitutes a majority of the directors, trustees or management of the private equity fund; or

(iv) Owns or controls more than 5 percent of any class of voting shares or similar interests in the private equity fund and is the investment adviser to the fund.

§ 225.174 What aggregate thresholds apply to merchant banking investments?

(a) *In general.* A financial holding company may not, without Board approval, directly or indirectly acquire any additional shares, assets or ownership interests under this subpart or make any additional capital contribution to any company the shares, assets or ownership interests of which are held by the financial holding company under this subpart if the aggregate carrying value of all merchant banking investments held by the financial holding company under this subpart exceeds:

(1) 30 percent of the Tier 1 capital of the financial holding company; or

(2) After excluding interests in private equity funds, 20 percent of the Tier 1 capital of the financial holding company.

(b) *How do these thresholds apply to a private equity fund?* Paragraph (a) of this section applies to the interest acquired or controlled by the financial holding company under this subpart in a private equity fund. Paragraph (a) of this section does not apply to any interest in a company held by a private equity fund or to any interest held by a person that is not affiliated with the financial holding company.

(c) *How long do these thresholds remain in effect?* This § 225.174 shall cease to be effective on the date that a final rule issued by the Board that specifically addresses the appropriate regulatory capital treatment of merchant banking investments becomes effective.

§ 225.175 What risk management, record keeping and reporting policies are required to make merchant banking investments?

(a) *What internal controls and records are necessary?*—(1) *General.* A financial holding company, including a private equity fund controlled by a financial holding company, that makes investments under this subpart must establish and maintain policies, procedures, records and systems reasonably designed to conduct, monitor and manage such investment activities and the risks associated with such investment activities in a safe and sound manner, including policies, procedures, records and systems reasonably designed to:

(i) Monitor and assess the carrying value, market value and performance of each investment and the aggregate portfolio;

(ii) Identify and manage the market, credit, concentration and other risks associated with such investments;

(iii) Identify, monitor and assess the terms, amounts and risks arising from transactions and relationships (including contingent fees or contingent interests) with each company in which the financial holding company holds an interest under this subpart;

(iv) Ensure the maintenance of corporate separateness between the financial holding company and each company in which the financial holding company holds an interest under this subpart and protect the financial holding company and its depository institution subsidiaries from legal liability for the operations conducted and financial obligations of each such company; and

(v) Ensure compliance with this part and any other provisions of law governing transactions and relationships with companies in which the financial holding company holds an interest under this subpart (*e.g.*, fiduciary principles or sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c, 371c–1), if applicable).

(2) *Availability of records.* A financial holding company must make the policies, procedures and records required by paragraph (a)(1) of this section available to the Board or the appropriate Reserve Bank upon request.

(b) *What periodic reports must be filed?* A financial holding company must provide reports to the appropriate Reserve Bank in such format and at such times as the Board may prescribe.

(c) *Is notice required for the acquisition of companies?*—(1) *Fulfillment of statutory notice requirement.* Except as required in paragraph (c)(2) of this section, no post-acquisition notice under section 4(k)(6) of the Bank Holding Company Act (12 U.S.C. 1843(k)(6)) is required by a financial holding company in connection with an investment

made under this subpart if the financial holding company has previously filed a notice under § 225.87 indicating that it had commenced merchant banking investment activities under this subpart.

(2) *Notice of large individual investments.* A financial holding company must provide written notice to the Board on the appropriate form within 30 days after acquiring more than 5 percent of the voting shares, assets or ownership interests of any company under this subpart, including an interest in a private equity fund, at a total cost to the financial holding company that exceeds the lesser of 5 percent of the Tier 1 capital of the financial holding company or $200 million.

§ 225.176 How do the statutory cross marketing and sections 23A and B limitations apply to merchant banking investments?

(a) *Are cross marketing activities prohibited?*—(1) *In general.* A depository institution, including a subsidiary of a depository institution, controlled by a financial holding company may not:

(i) Offer or market, directly or through any arrangement, any product or service of any company if more than 5 percent of the company's voting shares, assets or ownership interests are owned or controlled by the financial holding company pursuant to this subpart; or

(ii) Allow any product or service of the depository institution, including any product or service of a subsidiary of the depository institution, to be offered or marketed, directly or through any arrangement, by or through any company described in paragraph (a)(1)(i) of this section.

(2) *How are certain subsidiaries treated?* For purposes of paragraph (a)(1) of this section, a subsidiary of a depository institution does not include a financial subsidiary held in accordance with section 5136A of the Revised Statutes (12 U.S.C. 24a) or section 46 of the Federal Deposit Insurance Act. (12 U.S.C. 1831w), any company held by a company owned in accordance with section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.*; 12 U.S.C. 611 *et seq.*), or any company held by a small business investment company owned in accordance with the Small Business Investment Act of 1958 (15 U.S.C. 661 *et seq.*).

(3) *How do the cross marketing restrictions apply to private equity funds?* The restriction contained in paragraph (a)(1) of this section does not apply to:

(i) Portfolio companies held by a private equity fund that the financial holding company does not control; or

(ii) The sale, offer or marketing of any interest in a private equity fund, whether or not controlled by the financial holding company.

(b) *When are companies held under section 4(k)(4)(H) affiliates under sections 23A and B?*—(1) *Rebuttable presumption of control.* The following rebuttable presumption of control shall apply for purposes of sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c, 371c-1): if a financial holding company directly or indirectly owns or controls more than 15 percent of the total equity of a company pursuant to this subpart, the company shall be presumed to be an affiliate of any member bank that is affiliated with the financial holding company.

(2) *Request to rebut presumption.* A financial holding company may rebut this presumption by providing information acceptable to the Board demonstrating that the financial holding company does not control the company.

(3) *Presumptions that control does not exist.* Absent evidence to the contrary, the presumption in paragraph (b)(1) of this section will be considered to have been rebutted without Board approval under paragraph (b)(2) of this section if any one of the following requirements are met:

(i) No officer, director or employee of the financial holding company serves as a director, trustee, or general partner (or individual exercising similar functions) of the company;

(ii) A person that is not affiliated or associated with the financial holding company owns or controls a greater percentage of the equity capital of the portfolio company than the amount owned or controlled by the financial holding company, and no more than one officer or employee of the holding company serves as a director or trustee

(or individual exercising similar functions) of the company; or

(iii) A person that is not affiliated or associated with the financial holding company owns or controls more than 50 percent of the voting shares of the portfolio company, and officers and employees of the holding company do not constitute a majority of the directors or trustees (or individuals exercising similar functions) of the company.

(4) *Convertible instruments.* For purposes of paragraph (b)(1) of this section, equity capital includes options, warrants and any other instrument convertible into equity capital.

(5) *Application of presumption to private equity funds.* A financial holding company will not be presumed to own or control the equity capital of a company for purposes of paragraph (b)(1) of this section solely by virtue of an investment made by the financial holding company in a private equity fund that owns or controls the equity capital of the company unless the financial holding company controls the private equity fund as described in § 225.173(d)(4).

(6) *Application of sections 23A and B to U.S. branches and agencies of foreign banks.* Sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c, 371c–1) shall apply to all covered transactions between each U.S. branch and agency of a foreign bank that acquires or controls, or that is affiliated with a company that acquires or controls, merchant banking investments and—

(i) Any portfolio company that the foreign bank or affiliated company controls or is presumed to control under paragraph (b)(1) of this section; and

(ii) Any company that the foreign bank or affiliated company controls or is presumed to control under paragraph (b)(1) of this section if the company is engaged in acquiring or controlling merchant banking investments and the proceeds of the covered transaction are used for the purpose of funding the company's merchant banking investment activities.

§ 225.177 Definitions.

(a) *What do references to a financial holding company include?*—(1) Except as otherwise expressly provided, the term ''financial holding company'' as used in this subpart means the financial holding company and all of its subsidiaries, including a private equity fund or other fund controlled by the financial holding company.

(2) Except as otherwise expressly provided, the term ''financial holding company'' does not include a depository institution or subsidiary of a depository institution or any portfolio company controlled directly or indirectly by the financial holding company.

(b) *What do references to a depository institution include?* For purposes of this subpart, the term ''depository institution'' includes a U.S. branch or agency of a foreign bank.

(c) *What is a portfolio company?* A portfolio company is any company or entity:

(1) That is engaged in any activity not authorized for the financial holding company under section 4 of the Bank Holding Company Act (12 U.S.C. 1843); and

(2) Any shares, assets or ownership interests of which are held, owned or controlled directly or indirectly by the financial holding company pursuant to this subpart, including through a private equity fund that the financial holding company controls.

(d) *Who are the executive officers of a company?*—(1) An executive officer of a company is any person who participates or has the authority to participate (other than in the capacity as a director) in major policymaking functions of the company, whether or not the officer has an official title, the title designates the officer as an assistant, or the officer serves without salary or other compensation.

(2) The term ''executive officer'' does not include—

(i) Any person, including a person with an official title, who may exercise a certain measure of discretion in the performance of his duties, including the discretion to make decisions in the ordinary course of the company's business, but who does not participate in the determination of major policies of the company and whose decisions are limited by policy standards fixed by senior management of the company; or

(ii) Any person who is excluded from participating (other than in the capacity of a director) in major policymaking functions of the company by resolution of the board of directors or by the bylaws of the company and who does not in fact participate in such policymaking functions.

CONDITIONS TO ORDERS

§ 225.200 Conditions to Board's section 20 orders.

(a) *Introduction.* Under section 20 of the Glass-Steagall Act (12 U.S.C. 377) and section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1843(c)(8)), a nonbank subsidiary of a bank holding company may to a limited extent underwrite and deal in securities for which underwriting and dealing by a member bank is prohibited. Pursuant to the Securities Act of 1933 and the Securities Exchange Act of 1934, these so-called section 20 subsidiaries are required to register with the SEC as broker-dealers and are subject to all the financial reporting, anti-fraud and financial responsibility rules applicable to broker-dealers. In addition, transactions between insured depository institutions and their section 20 affiliates are restricted by sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1). The Board expects a section 20 subsidiary, like any other subsidiary of a bank holding company, to be operated prudently. Doing so would include observing corporate formalities (such as the maintenance of separate accounting and corporate records), and instituting appropriate risk management, including independent trading and exposure limits consistent with parent company guidelines.

(b) *Conditions.* As a condition of each order approving establishment of a section 20 subsidiary, a bank holding company shall comply with the following conditions.

(1) *Capital.* (i) A bank holding company shall maintain adequate capital on a fully consolidated basis. If operating a section 20 authorized to underwrite and deal in all types of debt and equity securities, a bank holding company shall maintain strong capital on a fully consolidated basis.

(ii) In the event that a bank or thrift affiliate of a section 20 subsidiary shall become less than well capitalized (as defined in section 38 of the Federal Deposit Insurance Act, 12 U.S.C. 1831o), and the bank holding company shall fail to restore it promptly to the well capitalized level, the Board may, in its discretion, reimpose the funding, credit extension and credit enhancement firewalls contained in its 1989 order allowing underwriting and dealing in bank-ineligible securities,[1] or order the bank holding company to divest the section 20 subsidiary.

(iii) A foreign bank that operates a branch or agency in the United States shall maintain strong capital on a fully consolidated basis at levels above the minimum levels required by the Basle Capital Accord. In the event that the Board determines that the foreign bank's capital has fallen below these levels and the foreign bank fails to restore its capital position promptly, the Board may, in its discretion, reimpose the funding, credit extension and credit enhancement firewalls contained in its 1990 order allowing foreign banks to underwrite and deal in bank-ineligible securities,[2] or order the foreign bank to divest the section 20 subsidiary.

(2) *Internal controls.* (i) Each bank holding company or foreign bank shall cause its subsidiary banks, thrifts, branches or agencies[3] to adopt policies and procedures, including appropriate limits on exposure, to govern their participation in transactions underwritten or arranged by a section 20 affiliate.

(ii) Each bank holding company or foreign bank shall ensure that an independent and thorough credit evaluation has been undertaken in connection with participation by a bank, thrift, or branch or agency in such transactions, and that adequate documentation of

[1] Firewalls 5–8, 19, 21 and 22 of *J.P. Morgan & Co., The Chase Manhattan Corp., Bankers Trust New York Corp., Citicorp, and Security Pacific Corp.*, 75 Federal Reserve Bulletin 192, 214–16 (1989).

[2] Firewalls 5–8, 19, 21 and 22 of *Canadian Imperial Bank of Commerce, The Royal Bank of Canada, Barclays PLC and Barclays Bank PLC*, 76 Federal Reserve Bulletin 158, (1990).

[3] The terms ''branch'' and ''agency'' refer to a U.S. branch and agency of a foreign bank.

that evaluation is maintained for review by examiners of the appropriate federal banking agency and the Federal Reserve.

(3) *Interlocks restriction.* (i) Directors, officers or employees of a bank or thrift subsidiary of a bank holding company, or a bank or thrift subsidiary or branch or agency of a foreign bank, shall not serve as a majority of the board of directors or the chief executive officer of an affiliated section 20 subsidiary.

(ii) Directors, officers or employees of a section 20 subsidiary shall not serve as a majority of the board of directors or the chief executive officer of an affiliated bank or thrift subsidiary or branch or agency, except that the manager of a branch or agency may act as a director of the underwriting subsidiary.

(iii) For purposes of this standard, the manager of a branch or agency of a foreign bank generally will be considered to be the chief executive officer of the branch or agency.

(4) *Customer disclosure*—(i) *Disclosure to section 20 customers.* A section 20 subsidiary shall provide, in writing, to each of its retail customers,[4] at the time an investment account is opened, the same minimum disclosures, and obtain the same customer acknowledgment, described in the Interagency Statement on Retail Sales of Nondeposit Investment Products (Statement) as applicable in such situations. These disclosures must be provided regardless of whether the section 20 subsidiary is itself engaged in activities through arrangements with a bank that is covered by the Statement.

(ii) *Disclosures accompanying investment advice.* A director, officer, or employee of a bank, thrift, branch or agency may not express an opinion on the value or the advisability of the purchase or the sale of a bank-ineligible security that he or she knows is being underwritten or dealt in by a section 20 affiliate unless he or she notifies the customer of the affiliate's role.

[4] For purposes of this operating standard, a retail customer is any customer that is not an ''accredited investor'' as defined in 17 CFR 230.501(a).

(5) *Intra-day credit.* Any intra-day extension of credit to a section 20 subsidiary by an affiliated bank, thrift, branch or agency shall be on market terms consistent with section 23B of the Federal Reserve Act.

(6) *Restriction on funding purchases of securities during underwriting period.* No bank, thrift, branch or agency shall knowingly extend credit to a customer secured by, or for the purpose of purchasing, any bank-ineligible security that a section 20 affiliate is underwriting or has underwritten within the past 30 days, unless:

(i) The extension of credit is made pursuant to, and consistent with any conditions imposed in a preexisting line of credit that was not established in contemplation of the underwriting; or

(ii) The extension of credit is made in connection with clearing transactions for the section 20 affiliate.

(7) *Reporting requirement.* (i) Each bank holding company or foreign bank shall submit quarterly to the appropriate Federal Reserve Bank any FOCUS report filed with the NASD or other self-regulatory organizations, and any information required by the Board to monitor compliance with these operating standards and section 20 of the Glass-Steagall Act, on forms provided by the Board.

(ii) In the event that a section 20 subsidiary is required to furnish notice concerning its capitalization to the Securities and Exchange Commission pursuant to 17 CFR 240.17a–11, a copy of the notice shall be filed concurrently with the appropriate Federal Reserve Bank.

(8) *Foreign banks.* A foreign bank shall ensure that any extension of credit by its branch or agency to a section 20 affiliate, and any purchase by such branch or agency, as principal or fiduciary, of securities for which a section 20 affiliate is a principal underwriter, conforms to sections 23A and 23B of the Federal Reserve Act, and that its branches and agencies not advertise or suggest that they are responsible for the obligations of a section 20 affiliate, consistent with section 23B(c) of the Federal Reserve Act.

[62 FR 45306, Aug. 27, 1997, as amended by Reg. Y, 63 FR 14804, Mar. 27, 1998]