§ 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

Subpart K—Proprietary Trading and Relationships With Hedge Funds and Private Equity Funds

SOURCE: 76 FR 8275, Feb. 14, 2011, unless otherwise noted.

§ 225.180 Definitions.

For purposes of this subpart:

(a) *Banking entity* means—

(1) Any insured depository institution;

(2) Any company that controls an insured depository institution;

(3) Any company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978; and

(4) Any affiliate or subsidiary of any of the foregoing entities.

(b) *Hedge fund* and *private equity fund* mean an issuer that would be an investment company, as defined in the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*), but for section 3(c)(1) or 3(c)(7) of that Act, or such similar funds as the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may, by rule, as provided in section 13(b)(2) of the Bank Holding Company Act (12 U.S.C. 1851(b)(2)), determine.

(c) *Insured depository institution* has the same meaning as given that term in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813), except that for purposes of this subpart the term shall not include an institution that functions solely in a trust or fiduciary capacity if—

(1) All or substantially all of the deposits of such institution are in trust

funds and are received in a bona fide fiduciary capacity;

(2) No deposits of such institution which are insured by the Federal Deposit Insurance Corporation are offered or marketed by or through an affiliate of such institution;

(3) Such institution does not accept demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others or make commercial loans; and

(4) Such institution does not—

(i) Obtain payment or payment related services from any Federal Reserve bank, including any service referred to in section 11A of the Federal Reserve Act (12 U.S.C. 248a); or

(ii) Exercise discount or borrowing privileges pursuant to section 19(b)(7) of the Federal Reserve Act (12 U.S.C. 416(b)(7)).

(d) *Nonbank financial company supervised by the Board* means a nonbank financial company supervised by the Board of Governors, as defined in section 102 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (12 U.S.C. 5311).

(e) *Board* means the Board of Governors of the Federal Reserve System.

(f) *Illiquid fund* means a hedge fund or private equity fund that:

(1) As of May 1, 2010—

(i) Was principally invested in illiquid assets; or

(ii) Was invested in, and contractually committed to principally invest in, illiquid assets; and

(2) Makes all investments pursuant to, and consistent with, an investment strategy to principally invest in illiquid assets.

(g) *Illiquid assets* means any real property, security, obligation, or other asset that—

(1) Is not a liquid asset;

(2) Because of statutory or regulatory restrictions applicable to the hedge fund, private equity fund or asset, cannot be offered, sold, or otherwise transferred by the hedge fund or private equity fund to a person that is unaffiliated with the relevant banking entity; or

(3) Because of contractual restrictions applicable to the hedge fund, private equity fund or asset, cannot be offered, sold, or otherwise transferred by the hedge fund or private equity fund for a period of 3 years or more to a person that is unaffiliated with the relevant banking entity.

(h) *Liquid asset* means:

(1) Cash or cash equivalents;

(2) An asset that is traded on a recognized, established exchange, trading facility or other market on which there exist independent, bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined for the particular asset almost instantaneously;

(3) An asset for which there are bona fide, competitive bid and offer quotations in a recognized inter-dealer quotation system or similar system or for which multiple dealers furnish bona fide, competitive bid and offer quotations to other brokers and dealers on request;

(4) An asset the price of which is quoted routinely in a widely disseminated publication that is readily available to the general public or through an electronic service that provides indicative data from real-time financial networks;

(5) An asset with an initial term of one year or less and the payments on which at maturity may be settled, closed-out, or paid in cash or one or more other liquid assets described in paragraphs (h)(1), (2), (3), or (4); and

(6) Any other asset that the Board determines, based on all the facts and circumstances, is a liquid asset.

(i) *Principally invested* and related definitions. A hedge fund or private equity fund:

(1) Is *principally invested* in illiquid assets if at least 75 percent of the fund's consolidated total assets are—

(i) Illiquid assets; or

(ii) Risk-mitigating hedges entered into in connection with and related to individual or aggregated positions in, or holdings of, illiquid assets;

(2) Is *contractually committed to principally invest* in illiquid assets if the fund's organizational documents, other documents that constitute a contractual obligation of the fund, or written representations contained in the fund's

offering materials distributed to potential investors provide for the fund to be principally invested in assets described in paragraph (i)(1) at all times other than during temporary periods, such as the period prior to the initial receipt of capital contributions from investors or the period during which the fund's investments are being liquidated and capital and profits are being returned to investors; and

(3) Has an *investment strategy to principally invest* in illiquid assets if the fund—

(i) Markets or holds itself out to investors as intending to principally invest in assets described in paragraph (i)(1) of this section; or

(ii) Has a documented investment policy of principally investing in assets described in paragraph (i)(1) of this section.

§ 225.181 Conformance Period for Banking Entities Engaged in Prohibited Proprietary Trading or Private Fund Activities.

(a) *Conformance Period*—(1) *In general.* Except as provided in paragraph (b)(2) or (3) of this section, a banking entity shall bring its activities and investments into compliance with the requirements of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart no later than 2 years after the earlier of:

(i) July 21, 2012; or

(ii) Twelve months after the date on which final rules adopted under section 13(b)(2) of the Bank Holding Company Act (12 U.S.C. 1851(b)(2)) are published in the FEDERAL REGISTER.

(2) *New banking entities.*—A company that was not a banking entity, or a subsidiary or affiliate of a banking entity, as of July 21, 2010, and becomes a banking entity, or a subsidiary or affiliate of a banking entity, after that date shall bring its activities and investments into compliance with the requirements of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart before the later of—

(i) The conformance date determined in accordance with paragraph (a)(1) of this section; or

(ii) Two years after the date on which the company becomes a banking entity or a subsidiary or affiliate of a banking entity.

(3) *Extended conformance period.* The Board may extend the two-year period under paragraph (a)(1) or (2) of this section by not more than three separate one-year periods, if, in the judgment of the Board, each such one-year extension is consistent with the purposes of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart and would not be detrimental to the public interest.

(b) *Illiquid funds*—(1) *Extended transition period.* The Board may further extend the period provided by paragraph (a) of this section during which a banking entity may acquire or retain an equity, partnership, or other ownership interest in, or otherwise provide additional capital to, a private equity fund or hedge fund if—

(i) The fund is an illiquid fund; and

(ii) The acquisition or retention of such interest, or provision of additional capital, is necessary to fulfill a contractual obligation of the banking entity that was in effect on May 1, 2010.

(2) *Duration limited.* The Board may grant a banking entity only one extension under paragraph (b)(1) of this section and such extension—

(i) May not exceed 5 years beyond any conformance period granted under paragraph (a)(3) of this section; and

(ii) Shall terminate automatically on the date during any such extension on which the banking entity is no longer under a contractual obligation described in paragraph (b)(1)(ii).

(3) *Contractual obligation.* For purposes of this paragraph (b)—

(i) A banking entity has a contractual obligation to take or retain an equity, partnership, or other ownership interest in an illiquid fund if the banking entity is prohibited from redeeming all of its equity, partnership, or other ownership interests in the fund, and from selling or otherwise transferring all such ownership interests to a person that is not an affiliate of the banking entity—

(A) Under the terms of the banking entity's equity, partnership, or other ownership interest in the fund or the banking entity's other contractual arrangements with the fund or unaffiliated investors in the fund; or

(B) If the banking entity is the sponsor of the fund, under the terms of a written representation made by the banking entity in the fund's offering materials distributed to potential investors;

(ii) A banking entity has a contractual obligation to provide additional capital to an illiquid fund if the banking entity is required to provide additional capital to such fund—

(A) Under the terms of its equity, partnership or other ownership interest in the fund or the banking entity's other contractual arrangements with the fund or unaffiliated investors in the fund; or

(B) If the banking entity is the sponsor of the fund, under the terms of a written representation made by the banking entity in the fund's offering materials distributed to potential investors; and

(iii) A banking entity shall be considered to have a contractual obligation for purposes of paragraph (b)(3)(i) or (ii) of this section only if—

(A) The obligation may not be terminated by the banking entity or any of its subsidiaries or affiliates under the terms of its agreement with the fund; and

(B) In the case of an obligation that may be terminated with the consent of other persons, the banking entity and its subsidiaries and affiliates have used their reasonable best efforts to obtain such consent and such consent has been denied.

(c) *Approval Required to Hold Interests in Excess of Time Limit*. The conformance period in paragraph (a) of this section may be extended in accordance with paragraph (a)(3) or (b) of this section only with the approval of the Board. A banking entity that seeks the Board's approval for an extension of the conformance period under paragraph (a)(3) or for an extended transition period under paragraph (b)(1) must—

(1) Submit a request in writing to the Board at least 180 days prior to the expiration of the applicable time period;

(2) Provide the reasons why the banking entity believes the extension should be granted, including information that addresses the factors in paragraph (d)(1) of this section; and

(3) Provide a detailed explanation of the banking entity's plan for divesting or conforming the activity or investment(s).

(d) *Factors governing Board determinations*—(1) *Extension requests generally*. In reviewing any application by a specific company for an extension under paragraph (a)(3) or (b)(1) of this section, the Board may consider all the facts and circumstances related to the activity, investment, or fund, including, to the extent relevant—

(i) Whether the activity or investment—

(A) Involves or results in material conflicts of interest between the banking entity and its clients, customers or counterparties;

(B) Would result, directly or indirectly, in a material exposure by the banking entity to high-risk assets or high-risk trading strategies;

(C) Would pose a threat to the safety and soundness of the banking entity; or

(D) Would pose a threat to the financial stability of the United States;

(ii) Market conditions;

(iii) The nature of the activity or investment;

(iv) The date that the banking entity's contractual obligation to make or retain an investment in the fund was incurred and when it expires;

(v) The contractual terms governing the banking entity's interest in the fund;

(vi) The degree of control held by the banking entity over investment decisions of the fund;

(vii) The types of assets held by the fund, including whether any assets that were illiquid when first acquired by the fund have become liquid assets, such as, for example, because any statutory, regulatory, or contractual restrictions on the offer, sale, or transfer of such assets have expired;

(viii) The date on which the fund is expected to wind up its activities and liquidate, or its investments may be redeemed or sold;

(ix) The total exposure of the banking entity to the activity or investment and the risks that disposing of, or maintaining, the investment or activity may pose to the banking entity or the financial stability of the United States;

(x) The cost to the banking entity of divesting or disposing of the activity or investment within the applicable period;

(xi) Whether the divestiture or conformance of the activity or investment would involve or result in a material conflict of interest between the banking entity and unaffiliated clients, customers or counterparties to which it owes a duty;

(xii) The banking entity's prior efforts to divest or conform the activity or investment(s), including, with respect to an illiquid fund, the extent to which the banking entity has made efforts to terminate or obtain a waiver of its contractual obligation to take or retain an equity, partnership, or other ownership interest in, or provide additional capital to, the illiquid fund; and

(xiii) Any other factor that the Board believes appropriate.

(2) *Timing of Board review.* The Board will seek to act on any request for an extension under paragraph (a)(3) or (b)(1) of this section no later than 90 calendar days after the receipt of a complete record with respect to such request.

(3) *Consultation.* In the case of a banking entity that is primarily supervised by another Federal banking agency, the Securities and Exchange Commission, or the Commodity Futures Trading Commission, the Board will consult with such agency prior to the approval of a request by the banking entity for an extension under paragraph (a)(3) or (b)(1) of this section.

(e) *Authority to impose restrictions on activities or investments during any extension period*—(1) *In general.* The Board may impose such conditions on any extension approved under paragraph (a)(3) or (b)(1) of this section as the Board determines are necessary or appropriate to protect the safety and soundness of the banking entity or the financial stability of the United States, address material conflicts of interest or other unsound banking practices, or otherwise further the purposes of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart.

(2) *Consultation.* In the case of a banking entity that is primarily supervised by another Federal banking agency, the Securities and Exchange Commission, or the Commodity Futures Trading Commission, the Board will consult with such agency prior to imposing conditions on the approval of a request by the banking entity for an extension under paragraph (a)(3) or (b)(1) of this section.

§ 225.182 Conformance Period for Nonbank Financial Companies Supervised by the Board Engaged in Proprietary Trading or Private Fund Activities.

(a) *Divestiture Requirement.* A nonbank financial company supervised by the Board shall come into compliance with all applicable requirements of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart, including any capital requirements or quantitative limitations adopted thereunder and applicable to the company, not later than 2 years after the date the company becomes a nonbank financial company supervised by the Board.

(b) *Extensions.* The Board may, by rule or order, extend the two-year period under paragraph (a) by not more than three separate one-year periods, if, in the judgment of the Board, each such one-year extension is consistent with the purposes of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart and would not be detrimental to the public interest.

(c) *Approval Required to Hold Interests in Excess of Time Limit.* A nonbank financial company supervised by the Board that seeks the Board's approval for an extension of the conformance period under paragraph (b) of this section must—

(1) Submit a request in writing to the Board at least 180 days prior to the expiration of the applicable time period;

(2) Provide the reasons why the nonbank financial company supervised by the Board believes the extension should be granted; and

(3) Provide a detailed explanation of the company's plan for conforming the activity or investment(s) to any applicable requirements established under section 13(a)(2) or (f)(4) of the Bank Holding Company Act (12 U.S.C. 1851(a)(2) and (f)(4)).

(d) *Factors governing Board determinations*—(1) *In general.* In reviewing any application for an extension under

paragraph (b) of this section, the Board may consider all the facts and circumstances related to the nonbank financial company and the request including, to the extent determined relevant by the Board, the factors described in § 225.181(d)(1).

(2) *Timing.* The Board will seek to act on any request for an extension under paragraph (b) of this section no later than 90 calendar days after the receipt of a complete record with respect to such request.

(f) *Authority to impose restrictions on activities or investments during any extension period.* The Board may impose conditions on any extension approved under paragraph (b) of this section as the Board determines are necessary or appropriate to protect the safety and soundness of the nonbank financial company or the financial stability of the United States, address material conflicts of interest or other unsound practices, or otherwise further the purposes of section 13 of the Bank Holding Company Act (12 U.S.C. 1851) and this subpart.

Subpart L—Conditions to Orders

SOURCE: 76 FR 8275, Feb. 14, 2011, unless otherwise noted.

§ 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

[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).