AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

Federal Register

Wednesday,
January 3, 2001

Part II

Federal Reserve System

12 CFR Part 225

Regulation Y; Docket Nos. R–1057 and R–1062; Bank Holding Companies and Change in Bank Control; Final Rule

FEDERAL RESERVE SYSTEM

12 CFR Part 225

Regulation Y; Docket Nos. R–1057 and R–1062; Bank Holding Companies and Change in Bank Control

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board of Governors of the Federal Reserve System has adopted a final rule that implements the financial holding company provisions of the Gramm-Leach-Bliley Act. This final rule replaces the interim rules governing financial holding companies that the Board adopted previously. The final rule describes the procedures a domestic bank holding company and a foreign banking organization must follow and the capital, management, and Community Reinvestment Act requirements they must meet in order to qualify as a financial holding company. The final rule also contains provisions that apply to a financial holding company that subsequently ceases to meet the applicable requirements.

In addition, the final rule lists the activities that the Gramm-Leach-Bliley Act defines as financial in nature and thereby authorizes a FHC to conduct. The final rule contains procedures that apply to a financial holding company that conducts those activities, a procedure that allows any interested party to request that the Board determine, in consultation with the Secretary of the Treasury, that additional activities are financial in nature or incidental to a financial activity and thus permissible for a financial holding company, and a procedure that allows a financial holding company to request the Board's prior approval to conduct an activity that is complementary to a financial activity.

The final rule also amends Regulation Y to define the term ''depository institution'' and to revise the existing definitions of the terms ''well capitalized'' and ''well managed,'' and makes conforming and other technical changes.

DATES: The final rule is effective February 2, 2001.

FOR FURTHER INFORMATION CONTACT: Scott G. Alvarez, Associate General Counsel (202/452–3583), Kathleen M. O'Day, Associate General Counsel (202/452–3786), Ann E. Misback, Assistant General Counsel (202/452–3788); Christopher W. Clubb, Senior Counsel (202/452–3904); Kieran J. Fallon, Senior Counsel (202/452–5270), or Adrianne G. Threatt, Senior Attorney (202/452–3554), Legal Division; or Betsy Cross, Deputy Associate Director (202/452–2574), Division of Banking Supervision and Regulation; Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC, 20551. For users of Telecommunications Device for the Deaf (''TDD''), contact Janice Simms at 202/452–4984.

SUPPLEMENTARY INFORMATION:

Background and Summary of Final Rule

The Gramm-Leach-Bliley Act (Pub. L. 106–102, 113 Stat. 1338 (1999)) (''GLB Act'') amended the Bank Holding Company Act (12 U.S.C. 1841 *et seq.*) (''BHC Act'') to allow a bank holding company that elects to become a FHC (a ''FHC'') and a foreign banking organization that elects to be treated as a FHC to engage in a broad range of financial activities, including securities underwriting, insurance sales and underwriting, and merchant banking. On January 18, 2000, the Board approved an interim rule implementing these provisions and detailing the procedures that allow a bank holding company and foreign banking organization to qualify for and maintain FHC status (65 FR 3786 (January 25, 2000)). This interim rule also enumerated the capital, management, and Community Reinvestment Act (12 U.S.C. 2901 *et seq.*) (''CRA'') requirements that must be satisfied in order to establish and maintain FHC status. On March 15, 2000, the Board amended the management criterion and certain provisions concerning the FHC election process applicable to foreign banking organizations. (65 FR 15053 (March 21, 2000)).

On March 10, 2000, the Board approved an additional interim rule containing a list of the financial activities that are permissible for a FHC to conduct. This interim rule also set forth the procedures a FHC must follow to engage in a financial activity; the process for requesting a Board determination that an additional activity is financial in nature or incidental thereto; and a procedure for requesting the Board's prior approval to engage in an activity that is complementary to a financial activity (65 FR 14433 (March 17, 2000)).

The interim rules on elections and activities both became effective on March 11, 2000, the effective date of the GLB Act, so that qualifying companies immediately could take advantage of the expanded powers granted by the statute. The vast majority of the provisions of the interim rules were included in a new subpart I of Regulation Y, entitled ''Financial Holding Companies.''

The Board solicited comment on the interim rules and received a total of 59 public comments on these rules. The commenters included bank holding companies and foreign banking organizations; state bank supervisory officials; trade associations representing the banking, insurance, and securities industries; foreign central banks and governmental officials; law firms; community groups; and individuals.

Many commenters supported the Board's interim rules and commended the Board for issuing the rules swiftly and using an easily comprehensible format. Commenters representing the interests of foreign banking organizations urged the Board to amend the FHC election procedures and requirements applicable to those organizations, including use of the leverage ratio in assessing comparability of capital, while domestic organizations asked the Board to hold foreign banking organizations to the same requirements that apply to U.S. bank holding companies. Commenters also were divided as to whether the Board should retain sections of the interim rules that reserved the Board's supervisory authority to impose restrictions on a bank holding company that met the statutory criteria to become a FHC but about which the Board nonetheless had supervisory concerns. Most comments regarding this section asserted that the Board did not have a statutory basis for imposing a requirement on a company that met the GLB Act's criteria to become a FHC. Several commenters also suggested that the Board should not require bank holding companies to submit supporting information with their FHC elections and that the Board should amend the definition of the term ''well managed.''

Commenters asked for guidance about the application of various aspects of the rule, including the interplay between Regulation Y and Regulation K with respect to activities conducted abroad by a FHC and the procedures for requesting to become a FHC as part of a section 3 proposal to become a bank holding company. A number of commenters suggested that the Board allow public comment on FHC declarations and condition the effectiveness of a FHC election on compliance with CRA-related requirements not enumerated in the GLB Act.

After carefully reviewing the public comments, the Board has adopted a final rule that largely incorporates the framework contained in the interim rules. The Board has made a number of

revisions in response to the public comments as well as revisions based on the experience of the Federal Reserve System in administering the interim rules since March 11, 2000. The suggestions made by commenters, the Board's responses thereto, and the Board's revisions are discussed in greater detail below.

Explanation of Final Rule

Section 225.81—What Is a FHC?

Consistent with the GLB Act, the interim rules defined a FHC as a bank holding company that meets the following requirements: (1) The company has made an effective election to become a FHC, and (2) all depository institutions controlled by the bank holding company are at the time of election and remain both well managed and well capitalized.[1] One commenter suggested that the Board allow a bank holding company that controls multiple banks to become a FHC if a depository institution representing a small percentage of the company's assets was not well managed. However, the GLB Act explicitly provides that a bank holding company may become a FHC only if each depository institution controlled by the company is well managed, and the Board cannot alter this requirement by regulation. Accordingly, the Board has adopted § 225.81 of the interim rule without amendment.

Definitions of Well Capitalized and Well Managed

As noted above, a bank holding company may become a FHC only if each of its subsidiary depository institutions is both well capitalized and well managed. The final rule, like the interim rule, provides that an *uninsured* depository institution is considered well capitalized if it meets or exceeds the capital ratios that its appropriate Federal banking agency has established under section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o) (''FDI Act'') for insured depository institutions.[2]

The final rule also amends and simplifies the existing definition of ''well managed'' in Regulation Y so that it can be used both for purposes of determining whether expedited processing of a bank holding company's application is appropriate and for determining whether a bank holding company qualifies to be a FHC. The final rule eliminates the requirement that a depository institution receive at least a satisfactory compliance rating to be deemed well managed, because the compliance criterion applies only to the availability of the expedited application process and not to an organization's status as a FHC. The rule amends the expedited processing procedures to adjust for these changes and to provide that a bank holding company's depository institutions must satisfy a compliance requirement for the bank holding company to qualify for expedited processing.[3] This revision does not change in any substantive way the application of the previous well managed criteria.

The FDI Act allows the appropriate Federal banking agency for a depository institution to use an examination conducted by a state banking agency in lieu of a Federal examination, provided the state examination meets the criteria at section 10(d) of the FDI Act (*see* 12 U.S.C. 1820(d)). To reflect this, the final rule allows the Board to rely on examinations conducted by the appropriate state agency where applicable in determining whether an institution is well managed.

Where a depository institution has not yet been examined, the final rule retains the provision of the interim rule that allows the Board to determine that the institution is well managed after reviewing the institution's managerial and other resources and consulting with the appropriate Federal banking agency for the institution. Moreover, the final rule provides that a depository institution resulting from the merger of two or more well managed depository institutions would be considered well managed unless the Board determined otherwise after consulting with the appropriate Federal banking agency. Commenters supported both these provisions.

Commenters requested additional guidance on whether a depository institution would remain well managed if it merged with an institution that was not well managed. In these circumstances, the Board believes that the managerial status of the combined institution likely would depend on the particular facts and circumstances. Accordingly, the final rule provides that an institution resulting from the merger of a well managed institution with an institution that is not well managed or that has not been examined will be considered well managed if the Board determines, after a review of managerial and other resources and after consulting the appropriate Federal banking agency, that the resulting institution is well managed.

Section 225.82—How Does a Bank Holding Company Elect to Become a FHC?

Section 225.82 sets forth the procedures that a bank holding company must follow to elect to become a FHC and describes when an election will and will not become effective. The rule allows a bank holding company to elect to become a FHC by filing a simple declaration with the appropriate Federal Reserve Bank. The declaration must contain a statement that the bank holding company elects to be a FHC; provide the name and head office addresses of the company and each of the depository institutions it controls; certify that each depository institution controlled by the company is well capitalized as of the date the company submits its declaration; provide the capital ratios as of the close of the previous quarter for each depository institution controlled by the company; and certify that each depository institution controlled by the company is well managed as of the date the company submits its declaration. In light of its experience with declarations under the interim rule, the Board has amended § 225.82 to clarify that a declaration is not deemed complete and the 30-day processing period for the declaration does not commence until the declaration contains all of the information required by § 225.82(b).

Several commenters requested that the Board eliminate the requirement that a declaration include capital ratio information because the Board already has access to capital data about depository institutions. However, the Board has retained this requirement for several reasons. The Board's experience administering the interim rule indicated that the capital data received from bank holding companies at times is different than the capital data otherwise available to the Board, particularly in the weeks immediately following the end of a quarter. In several cases, the capital information provided by a bank holding company was more favorable than the data otherwise available to the Board and thus resulted in an effective FHC election that the Board's data alone would not have supported. Moreover, the Board's experience suggests that

[1] Section 225.81 also sets forth the provisions that apply to a foreign bank that controls a depository institution in the United States, as well as U.S. bank holding companies that control a foreign bank with U.S. operations. These provisions are described in more detail below in the discussion of §§ 225.90 to 225.93.

[2] The final rule also defines the term ''depository institution'' at § 225.2(t) using the definition provided at section 2 of the BHC Act as amended by the GLB Act. For purposes of Regulation Y, 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)).

[3] *See* 12 CFR 225.14 and 225.23, as amended by this rule.

requiring a bank holding company to submit the capital data may improve the quality of declarations submitted to the Board because it aids the company in determining whether it can in fact certify that all of its subsidiary depository institutions are well capitalized.

Section 225.82(f) of the final rule provides that a bank holding company's election to become a FHC becomes effective on the 31st day after the date that the declaration was received unless the Board notifies the company prior to that time the election is ineffective. The rule also provides that the Board or the appropriate Federal Reserve Bank affirmatively may notify a company that its election is effective prior to the expiration of the 30-day review period.

CRA Requirement

For a bank holding company's FHC election to be effective, the final rule requires the Board to determine that each insured depository institution controlled by the bank holding company has achieved a rating of at least ''satisfactory record of meeting community credit needs'' at its most recent examination under the CRA. Consistent with the GLB Act, the final rule also allows the Board, when evaluating the CRA criterion, to exclude an insured depository institution that a bank holding company acquired in the 12 months prior to submitting its FHC declaration. To qualify for this exclusion, the company must submit and the appropriate Federal banking agency for the insured depository institution must accept a plan to restore the institution's CRA rating to a satisfactory level.

Commenters asked for clarification about how the Board in practice would apply the CRA requirement. In particular, commenters requested guidance on whether a bank holding company that controls an institution that has not been examined may make an effective FHC election. The GLB Act states that the Board must find a FHC election to be ineffective if not all of the subsidiary insured depository institutions of the company have achieved at least a satisfactory CRA rating at its ''most recent examination.'' In light of this statutory language, the final rule allows a bank holding company to qualify as a FHC if it controls an institution that has not been examined for CRA compliance and thus has not yet achieved any CRA rating, provided that the company meets all other applicable criteria. As with any other insured depository institution, if an unrated institution does not achieve at least a satisfactory rating at its next CRA examination, the FHC would be subject to the limitations that apply under § 225.84.

A number of commenters requested the Board, when determining whether the insured depository institutions controlled by a bank holding company have met the CRA requirement, to (1) publish FHC declarations for comment, particularly when the Board excludes a recently acquired institution; (2) take into account additional facts related to the CRA record of a bank holding company and the insured depository institutions it controls; and (3) condition the effectiveness of a FHC election on a company's compliance with various CRA-related criteria not mentioned in the GLB Act.

The GLB Act establishes the requirements that a bank holding company must meet to become a FHC and sets forth a detailed framework that limits the Board's evaluation of the CRA criterion. The GLB Act provides that the Board must find a bank holding company's election to be ineffective only if all of the insured depository institutions controlled by the company, except for an institution that qualifies for the limited exclusion discussed above, have not achieved an overall CRA rating that was at least satisfactory.[4] The GLB Act specifically ties the CRA requirement to the CRA examination rating of each insured depository institution and neither provides for public comment on FHC elections nor authorizes the Board to condition the effectiveness of an election based on the CRA criterion. The Board therefore believes that incorporating the suggestions mentioned above would be inconsistent with the terms of the GLB Act and, accordingly, has not amended the rule as suggested.

Proposals To Become a Bank Holding Company and a FHC

The final rule allows a company that is not a bank holding company to submit simultaneously an application under section 3(a)(1) of the BHC Act to become a bank holding company and a request to become a FHC on consummation of that transaction. The process applicable to simultaneous filings to become both a bank holding company and a FHC is included in a new § 225.82(f). The FHC request must (1) state that the company seeks to become a FHC on consummation of its section 3 proposal to become a bank holding company and (2) certify that each depository institution that would be controlled by the company on consummation of the section 3 proposal will be both well capitalized and well managed on the date of consummation.

In order to coordinate action on these two requests, the final rule delays the official acceptance of the FHC declaration to the date the company consummates its section 3 proposal and becomes a lawful bank holding company. The Board generally will find this declaration effective on the date the company becomes a bank holding company through consummation of its section 3 proposal to become a bank holding company. However, the rule provides that a declaration will not be effective if the Board determines that (1) a depository institution that would be controlled by the company on consummation of its section 3 proposal is not both well capitalized and well managed; or (2) any insured depository institution to be controlled by the company on consummation did not achieve at least a satisfactory rating at its most recent CRA examination. The Board may make this determination at any time prior to the date the company becomes a bank holding company. Unless the Board determines otherwise based on the specific facts of the case, a company that becomes a bank holding company by acquiring an insured depository institution with a poor CRA rating cannot attain an effective FHC election until the acquired institution achieves at least a satisfactory CRA rating.

The Board's Ability To Take Supervisory Action

Section 225.82(d) of the interim rule on elections noted that the Board retained authority to take supervisory actions against a bank holding company that had made an effective election to become a FHC. These actions could, for example, include imposing supervisory limits on the activities and acquisitions of a FHC. Although one commenter supported this provision, several commenters asserted that the Board did not have statutory authority to limit the operations of a FHC that met the applicable statutory criteria.

Section 8 of the BHC Act, section 8 of the Federal Deposit Insurance Act, and other applicable statutes long have given the Board supervisory authority to restrict the conduct of bank holding companies where necessary or appropriate to protect the safety and

[4] The Board notes that it cannot exclude a recently acquired institution with a poor CRA rating unless the appropriate Federal banking agency for the institution has accepted an affirmative correction plan to restore the institution's CRA rating to at least a satisfactory level. Thus, the company's CRA correction plan for the institution must be reviewed carefully by both the institution's primary Federal regulator and the Board.

soundness of depository institutions or otherwise further the purpose of Federal banking laws. Although the GLB Act amended several of these provisions, it did not limit the general applicability of the Board's supervisory power over bank holding companies that become financial holding companies. Therefore, the final rule continues to provide that the Board may take appropriate supervisory action against a FHC if the Board believes that the company does not have the appropriate financial and managerial resources to commence or conduct an activity, make an acquisition, or retain ownership of a company, or the Board believes such action is appropriate to enforce applicable Federal law.

Section 225.83—What Are the Consequences of Failing to Continue To Meet Applicable Capital and Management Requirements?

Under the GLB Act, a FHC is subject to special corrective action requirements if any depository institution controlled by the company ceases to be both well capitalized and well managed. Section 225.83 of the rule implements these provisions.

The Board received comments about a variety of aspects of § 225.83. Several commenters requested that the Board clarify when and under what circumstances a company must provide notice to the Board of a change in the capital or management status of a subsidiary depository institution. Some commenters questioned the Board's authority and decision to require a company that it is subject to a corrective action agreement to obtain the Board's prior approval to engage in an additional activity or acquires shares of any company under section 4(k). Other commenters suggested that a FHC should be allowed to acquire an institution that is less than well managed without thereafter being subject to the prior approval requirement.

After carefully considering these comments and the Board's experience in administering the interim rule, the Board has adopted a final rule that retains the substantive provisions of § 225.83. This final rule contains the following modifications.

First, because a FHC may have access to capital and managerial data on its subsidiaries before the Board does, the final rule requires that a FHC notify the Board within 15 days of becoming aware that any of its subsidiary depository institutions has ceased to be well capitalized or well managed. The Board has amended § 225.83(b) to provide that a company becomes aware that a subsidiary depository institution is not well capitalized upon the occurrence of any material event that would change the capital category assigned to the institution for purposes of section 38 of the FDI Act (12 U.S.C. 1831o). These are the same events that would trigger a depository institution to provide notice to its appropriate Federal banking agency under the prompt corrective action rules (*see, e.g.*, 12 CFR 208.42(b) and (c)). A company is deemed to become aware that a subsidiary depository institution is no longer well managed at the time the depository institution receives written notice from its appropriate Federal banking agency that either the institution's composite rating or management rating is not at least satisfactory. The final rule also provides that this notice may come from the state banking agency in an examination conducted in accordance with section 10(d) of the FDI Act.

As noted above, the GLB Act specifically authorizes the Board to impose limitations on the conduct or activities of a company that is subject to a corrective action agreement if the Board believes that such limitations are appropriate under the circumstances and consistent with the purposes of the BHC Act. The Board believes it is appropriate and consistent with the purposes of the BHC Act to require a FHC that ceases to meet applicable capital and management standards to obtain the Board's approval prior to conducting any of the activities that are newly authorized for FHCs by the GLB Act. This allows the Board to assure that the FHC is not inappropriately diverting resources from improving the condition of its subsidiary depository institutions. It also recognizes that the new powers and streamlined review process contained in the GLB Act were intended to be available only to companies that maintain strong capital and management at their subsidiary depository institutions. For these reasons, the final rule retains the prior approval requirement for companies subject to a corrective action agreement.

The Board may determine to grant approval to engage in additional activities on a general basis or only on a transaction-by-transaction basis as appropriate, given the circumstances that caused the FHC to fail to meet the well capitalized and well managed requirements. For example, the Board has given general approval to a FHC that controlled only well capitalized and well managed institutions and then acquired a relatively small troubled institution and immediately developed a plan to improve the condition of the troubled institution.

The final rule retains the requirement that a company that received notice from the Board that one or more of its subsidiary depository institutions is not both well capitalized and well managed execute an agreement with the Board to comply with the capital and management requirements applicable to financial holding companies (a ''corrective action agreement''). This corrective action agreement must be executed within 45 days of the company's receipt of the notice or such additional time as the Board may allow if a company requests an extension of time, must explain the actions the company will take to correct all areas of noncompliance and the time frame within which each action will be take, must provide any other information the Board may require, and must be acceptable to the Board.

If a company subject to a corrective action agreement does not cause all of its subsidiary depository institutions to be well capitalized and well managed within 180 days (or such other time as the Board may permit) of receiving notice of a deficiency from the Board, the Board may order the company to divest ownership or control of any depository institution the company owns or controls. The GLB Act and the final rule state that a company may comply with a Board order to divest by ceasing to engage in any activity that may be conducted only under sections 4(k), 4(n), or 4(o) of the BHC Act.[5]

Section 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?

The GLB Act requires the Board to prohibit a FHC from engaging in or acquiring control of a company engaged in any new activity under sections 4(k) and 4(n) of the BHC Act if any insured depository institution controlled by the FHC has received a rating of less than ''satisfactory record of meeting community credit needs'' in its most recent CRA examination. Section 225.84 implements this provision by providing that the statutory prohibitions apply

[5] The interim rule provided that a company could choose to comply with an order to divest by ceasing to engage in any activity that would not be permissible for a bank holding company under section 4(c)(8) of the BHC Act. The Board has changed the statutory reference in order to clarify that a company that complies with a divestiture order by ceasing to engage in certain activities may continue to engage in any conduct permissible for a bank holding company under section 4(c), not just the conduct permitted by section 4(c)(8).

upon receipt by the FHC of notice that any subsidiary insured depository institution has received a less-than-satisfactory CRA rating.

Section 225.84 provides that a FHC receives notice of a less-than-satisfactory CRA rating when (1) an insured depository institution controlled by the FHC receives written notice from its appropriate Federal banking agency that the institution has received a less-than-satisfactory CRA performance rating at its most recent examination; or (2) the FHC receives written notice from the Board that an insured depository institution it controls has received such a rating. The prohibitions imposed by § 225.84 remain in effect until each insured depository institution controlled by the FHC has received at least a satisfactory CRA rating at its most recent examination.

The Board also has considered the applicability of the CRA provisions to the situation in which a FHC acquires an insured depository institution with a poor CRA rating. The terms of the GLB Act require that the Board apply the prohibitions if ''any insured depository institution subsidiary of such FHC * * * has received in its most recent examination under the CRA a rating of less than 'satisfactory record of meeting community credit needs.' '' The Board believes that this language is best read to apply only when an insured depository institution receives a less-than-satisfactory CRA rating while it is under the control of the FHC.[6] A FHC is responsible for the CRA rating of an insured depository institution only if the FHC controlled the institution during the period that the examination occurs. Moreover, it would discourage FHCs with well rated institutions from acquiring and correcting poorly rated institutions if a penalty were imposed on the FHC immediately upon acquiring the poorly rated institution. The Board believes that there are strong public benefits in allowing a bank holding company with a proven CRA performance record at its existing insured depository institutions to acquire a poorly rated insured depository institution.

Accordingly, the final rule retains the provisions of the interim rule that provide that the CRA prohibitions apply to a FHC when an insured depository institution that is controlled by the FHC receives notice from the appropriate Federal banking agency that the insured depository institution has received a less-than-satisfactory CRA rating. This notice typically will occur, if at all, at the first CRA examination after the poorly rated insured depository institution is acquired by the FHC. If the institution does not achieve at least a satisfactory CRA rating at its first CRA examination following the acquisition, the prohibitions would apply to the FHC. This interpretation is consistent with the provision of the GLB Act that allows the Board when evaluating a FHC election to exclude the poor rating of any institution acquired by the company within the preceding 12 months.

The Board will monitor the FHC's progress in addressing the CRA performance of any recently acquired insured depository institution and reserves the right also to provide notice that the CRA prohibitions apply if the FHC is not taking appropriate action to improve the insured depository institution's CRA performance.

The rule states that a FHC's ability to engage in certain activities is not affected while the prohibitions are in effect. First, consistent with the GLB Act, a FHC that notified the Board it was engaged in merchant banking or insurance company investment activities prior to the time one of its subsidiary insured depository institutions received a less-than-satisfactory CRA rating may continue to make investments in the ordinary course of conducting such investment activities. Second, a FHC may engage in activities and make acquisitions under section 4(c)(8) of the BHC Act, subject to the applicable notice and approval requirements.

Section 225.85—Is Notice To or Approval From the Board Required Prior to Engaging in a Financial Activity?

Section 225.85 of the final rule generally permits a FHC to commence any financial activity or acquire control of a company engaged exclusively in one or more financial activities without the Board's prior approval.[7] The final rule specifically provides that a FHC may conduct any financial activity either in the United States or abroad, subject to the laws of the jurisdiction in which the activity is conducted.

Consistent with the GLB Act, § 225.85 of the final rule provides that a FHC must obtain prior Board approval to acquire more than 5 percent of the shares of a savings association. In addition, for the reasons explained above, the rule notes that the Board, in the exercise of its supervisory authority, may require a FHC to obtain prior Board approval to engage in or acquire a company engaged in a financial activity. In each of these cases, the final rule adopts the provisions of the interim rule with only minor, technical revisions.[8]

Section 225.85(a)(3) of the interim rule also allowed a FHC to control or acquire more than 5 percent of the voting shares of a financial company that engaged in limited nonfinancial activities if certain conditions were met, including the condition that the acquired company be substantially engaged in activities that are permissible for a FHC. The Board has revised this provision in several respects in light of its experience administering the interim rule. First, the Board has clarified that the acquired must be substantially engaged in activities that are financial in nature, incidental to a financial activity, or otherwise permissible for a FHC under section 4(c) of the BHC Act.[9] The final rule provides that a company generally is considered to be ''substantially engaged'' in permissible activities if at least 85 percent of the company's consolidated total annual gross revenues and 85 percent of the company's consolidated total assets are attributable to the conduct of financial and incidental activities and other activities that are permissible under section 4(c) of the BHC Act.

Although a FHC may acquire any percentage of shares or control of a company engaged in limited impermissible activities, the FHC need only provide a post-transaction notice under § 225.87 if such an acquisition results in control of the company. The final rule continues to require that the FHC conform, terminate, or divest all of

[6] Moreover, although the GLB Act requires the Board to impose prohibitions on the activities and acquisitions of a FHC if an insured depository institution of the FHC has received a less-than-satisfactory rating at its most recent CRA examination, the statute does not enumerate a specific procedure or time frame within which the Board must implement this requirement.

[7] The term ''financial activities'' refers to activities that have been determined to be financial in nature or incidental to a financial activity either by the GLB Act or by the Board in consultation with the Secretary of the Treasury. A list of financial activities is included at § 225.86 of the rule.

[8] For example, the rule clarifies that a FHC must obtain prior Board approval to acquire control or more than 5 percent of the shares of a company that owns, operates, or controls a savings association.

[9] Complementary activities are subject to prior approval on a case-by-case basis under section 4(j) of the BHC Act and, therefore, a company engaged in complementary activities generally could not be acquired using the post-transaction notice procedure. Consequently, complementary activities have not been included for the purpose of determining whether a company with mixed activities meets the requirement that it be substantially engaged in permissible activities for FHCs.

the acquired companies impermissible activities within two years of the acquisition. A commitment to terminate impermissible activities is unnecessary, because, under the final rule as written, an acquisition would be unauthorized if the activities of the company are not conformed to Regulation Y within two years of the acquisition.

Section 225.86—What Activities Are Permissible for a FHC?

Section 225.86 of the rule provides a list of the activities that the GLB Act defines as financial in nature and thus permissible for a FHC to conduct directly or indirectly.

Activities Previously Determined To Be Closely Related to Banking

Subsection (a)(1) permits a FHC to conduct any activity that the Board had determined by regulation or order prior to November 12, 1999, to be so closely related to banking as to be a proper incident thereto under section 4(c)(8) of the BHC Act. These activities are listed in § 225.28 of Regulation Y, and the rule incorporates these activities through a cross-reference to that section.

Subsection (a)(2) specifically lists each of the activities the Board approved by order as closely related to banking prior to November 12, 1999, and provides a citation to the most recent or the most comprehensive Board order concerning the activity. These activities are: Providing administrative and other services to mutual funds; owning shares of a securities exchange; providing employment histories to third parties; check cashing and wire transmissions services; providing notary public services, selling postage stamps and postage-paid envelopes; providing vehicle registration services, and selling public transportation tickets and tokens in connection with offering banking services; and real estate title abstracting. The interim rule on activities also authorized financial holding companies to act as a certification authority for digital signatures. The final rule clarifies that this activity includes authenticating the identity of persons conducting financial and nonfinancial transactions abroad, which is consistent with the scope of activities approved by the relevant Board order (*See Bayerische Hypo-und Vereinsbank AG, et al.,* 86 Federal Reserve Bulletin 56 (2000)).

Financial holding companies that engage in any activity pursuant to paragraph (a) must conduct the activity in accordance with the terms and conditions contained in Regulation Y and the Board's orders authorizing the activity, unless such terms and conditions are modified by the Board.[10] Some commenters requested that the Board amend the rule to include a description of the conditions and limitations governing the conduct of each activity listed in subsection (a). The Board notes that the conditions and limits governing the activities listed in subsection (a) are set forth in § 225.28 of Regulation Y or in the orders referenced in § 225.28(a)(2), and the Board believes that adding a list of conditions and limitations to the rule would lengthen the rule without significantly facilitating compliance with it. Where companies have questions concerning the conditions or limitations applicable to an activity, the company may contact the Board or appropriate Reserve Bank.

Activities Usual in Connection With the Transaction of Banking Abroad

The GLB Act also defined as financial in nature 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* 12 CFR 211.5(d)). Subsection (b) lists the three activities that the Board had determined to be usual in connection with the transaction of banking abroad that are not otherwise defined as financial in nature by other provisions of the GLB Act. These activities are management consulting (beyond that which is allowed under § 225.28 and incorporated by reference at section 225.86(a)(1)); operating a travel agency in connection with the offering of financial services; and organizing and sponsoring a mutual fund.[11] These activities must be conducted in accordance with the limitations set forth in Regulation K regarding the scope and conduct of the activity.[12]

The GLB Act authorizes financial holding companies to conduct the activities listed at § 211.5(d) of Regulation K that, prior to the GLB Act, a bank holding company could conduct abroad. One commenter stated that the activity list at § 225.86(b) should include ''commercial and other banking activities,'' which is the activity described at § 211.5(d)(1) of Regulation K. As a general matter, the GLB Act was intended to expand the range of nonbanking activities that a FHC could conduct and was not meant to affect the provisions of the BHC Act relating to the conduct of banking activities. Specifically, the GLB did not amend the prior approval requirement at section 3 of the BHC Act that governs the acquisition by a bank holding company, including a FHC, of a domestic bank. The Board therefore believes that the GLB Act did not authorize a FHC to conduct commercial and other banking activities in the United States by using the post-transaction notice procedure. In addition, the Board believes that a FHC's acquisition of a foreign bank should continue to be subject to the procedures set forth in Regulation K in order to ensure that the Board fulfills its responsibilities as home country supervisor in relation to international expansion of U.S. banking organizations, consistent with the standards established by the Basel Committee on Banking Supervision (Basel Committee). Accordingly, the Board has not included commercial and other banking activities on the activities list at § 225.86 that may be conducted by using the post-transaction notice procedure.

Other Activities Defined as Financial in Nature by the GLB Act

In addition to authorizing activities that the Board previously has authorized a bank holding company to conduct, the GLB defines several other activities as financial in nature. These activities, which are listed at sections 4(k)(4)(A)–(E), (H), and (I) of the BHC Act, include acting as principal, agent or broker in the sale of insurance products (including annuities and reinsurance products); underwriting, dealing in, and making a market in securities without any limitation on revenues that can be derived from bank ineligible securities; and merchant banking an insurance

[10] The Board by order has authorized bank holding companies under section 4(c)(8) to underwrite and deal in bank-ineligible securities provided that the company does not derive more than 25 percent of its revenues from such activities. *See J.P. Morgan & Co., Incorporated,* 75 Federal Reserve Bulletin 192 (1989). The list in subsection (a)(2) does not include underwriting and dealing in bank-ineligible securities, however, because financial holding companies may conduct these activities under section 4(k)(4)(E) of the BHC Act without regard to the 25-percent revenue limit. Some commenters requested that the Board also remove the 25-percent revenue limit applicable to the conduct of securities underwriting and dealing activities by bank holding companies under section 4(c)(8) of the BHC Act. In the GLB Act, Congress authorized only those bank holding companies that meet the capital, management and CRA standards applicable to financial holding companies to engage in expanded securities activities. The Board does not believe at this time that it would be appropriate to allow bank holding companies that do not meet these standards to engage in expanded securities activities.

[11] Section 4(k)(4)(G) and the rule do not authorize a FHC to engage in activities that the Board authorized a bank holding company to provide in individual orders issued under section 4(c)(13) of the BHC Act.

[12] As discussed more thoroughly below, the notice procedures in Regulation K do not apply to activities that are conducted under section 4(k)(4) of the BHC Act and Regulation Y.

company investment activities. Subsection 225.86(c) provides that a FHC may engage in any activity set forth in the above-referenced sections of the BHC Act. These activities must be conducted in accordance with applicable restrictions and limitations contained in the GLB Act and any implementing regulations or supervisory guidance adopted by the Board.[13]

Several commenters on the interim rule requested that the Board amend section 225.86 to eliminate cross references to the GLB Act and other sections of Regulation Y and to provide a complete description of each activity permissible for a FHC, including the conditions and limitations applicable to that activity. The Board believes the activities incorporated in the rule by reference are easily located elsewhere in the Board's Regulation Y and the BHC Act, and that including the requested provisions in the rule would lengthen the rule without adding a commensurate level of convenience. Accordingly, the Board has not included the requested provisions in the final rule. The Board has, however, prepared a single list of all activities permitted under section 225.86 that may be obtained from the Reserve Banks.

The GLB Act directs the Board, by regulation or order, to define the extent to which three activities listed in section 4(k)(5) are financial in nature or incidental to a financial activity. The Board anticipates proposing a rule to implement section 4(k)(5) in the near future.

The GLB Act also permits the Board, in consultation with the Secretary of the Treasury, to determine that additional activities not listed in section 225.86 are financial in nature of incidental thereto. In this regard, the Board recently determined by rule that acting as a finder is an activity that is incidental to a financial activity (*see* 65 FR 80735 (December 22, 2000)). The Board also has requested comment on a proposal to allow FHCs, as an activity that is complementary to a financial activity, to invest in companies engaged in certain data processing and Internet-related activities (see 65 FR 80384 (December 21, 2000)).

Interplay Between § 225.86 and Other Authorities

Although the Board is not listing each limitation and condition that applies to the activities described at § 225.86, the Board believes that some general guidance on the how the limitations apply is warranted in light of a number of public comments and informal inquiries received by Board staff on this subject. As the Board previously has indicated in connection with issuing the interim rules, the various sections that authorize activities for bank holding companies and financial holding companies, most notably sections 4(c)(8), 4(c)(13), and 4(k), remain separate sources of authority under which a FHC may engage in various activities. If an activity is listed in more than one provision of section 4, the FHC may choose to conduct the activity under any applicable provision, subject only to the procedures and limitations that the chosen source of authority imposes on the activity.

For example, a FHC that wishes to engage in securities underwriting could choose to conduct that activity under section 4(c)(8). If it chose that source of authority, the FHC would be required to obtain prior Board approval under subpart C of Regulation Y and would be required to conduct the underwriting activity subject to the revenue restrictions and other limitations applicable to securities underwriting activities conducted under section 4(c)(8). Alternatively, a FHC could engage in securities underwriting under section 4(k)(4)(E), in which case only a post-transaction notice would be required and the limitations of section 4(c)(8) would not apply to the activity.

As discussed above, the final rule states that a FHC may conduct any activity listed at § 225.86 either in the United States or abroad using the post-transaction notice procedure.[14] As with the conduct of financial activities in the United States, the limitations that apply to an activity conducted abroad by a FHC depend on the legal authority under which the FHC conducts the activity. If the FHC conducts an activity abroad under section 4(c)(13) of the BHC Act as implemented by § 211.5(d) of Regulation K, all the requirements and investment limitations described in § 211.5 would apply. If, however, a FHC conducts an activity listed at 4(c)(13) abroad using section 4(k)(4)(G) of the BHC Act, which incorporates by reference the activities authorized by the Board under section 4(c)(13), the Regulation K general consent procedures and investment limitations do not apply.

Section 225.87—Is Notice to the Board Required After Engaging in a Financial Activity?

Section 225.87(a) of the final rule describes when a FHC must provide notice to the Board after commencing or acquiring a company engaged in a permissible financial activity. As a general matter, the final rule states that a FHC may engage in any activity listed in § 225.86 by providing the appropriate Reserve Bank with a notice within 30 days of commencing the activity or acquiring control of a company engaged in the activity. The interim rule provided that this notice could take the form of a letter that contained information about the activity commenced and the company that conducts it. In response to public comments and to ensure that the post-transaction notices contain the basic information necessary for the Board to monitor a FHC's activities, the Board has designated forms that domestic and foreign financial holding companies must use to satisfy the post-transaction notice requirement.[15] The authorized form requires limited information about the activity commenced or the company acquired, as well as information about the location of the company conducting the activity and its status within the FHC's organization structure. The appropriate form for submitting the post-transaction notice may be obtained from any Federal Reserve Bank or from the Board.

Section 225.87(b) of the final rule outlines the exceptions under which post-transaction notice is not required to engage in an activity or make an acquisition. Consistent with the GLB Act, no notice is required in connection with the acquisition of shares of a company if the FHC would not control

[13] For example, the Board, in conjunction with the Secretary of the Treasury, adopted and requested public comment on an interim rule implementing the merchant banking investment provisions of the GLB Act. See 65 FR 16460 (March 28, 2000).

[14] The GLB Act states that a FHC may conduct *in the United States* those activities previously authorized by the Board at § 211.5(d) of Regulation K (emphasis added). The Board has received several inquiries as to whether a FHC also may conduct these activities outside the United States using the post-transaction notice. The GLB Act generally intended to authorize FHCs to conduct all of the activities it defined as financial in nature in the United and abroad using the streamlined procedure. Moreover, all but the three Regulation K activities listed separately at § 225.86(b) have been authorized in the same form under Regulation Y. The preexisting Regulation Y activities authorized for FHCs do not have the ''in the United States'' reference and may be conducted abroad using the streamlined procedure. The Board has determined, as reflected in this final rule, that no regulatory purpose would be served by requiring a FHC to follow the more restrictive Regulation K procedures to conduct the remaining three listed activities abroad. An FHC therefore may conduct all activities listed at § 225.86 either in the United States or abroad using the post-transaction notice procedure.

[15] Domestic financial holding companies should use the FR Y–6A, which soon will be replaced by the FR Y–10, and foreign banking organizations should use the FR Y–7A, which soon will be replaced by the FR Y–10F.

the company after the acquisition. The final rule retains this provision.

The rule also provides that a FHC that properly has notified the appropriate Federal Reserve Bank that the FHC is engaged in securities underwriting and dealing, merchant banking, or insurance company investment activities generally is not required to provide an additional post-transaction notice when the FHC makes particular investments in the ordinary of course of conducting those activities. Notwithstanding this exception for individual investments, investments in more than 5 percent of the shares, assets, or other ownership interests of a company that have a cost that exceeds the lesser of 5 percent of the FHC's Tier I capital or $200 million must be reported under § 225.87. In response to comments that the provisions of the interim rule on activities related to merchant banking investments were difficult to understand, the Board has restructured those provisions to explain more succinctly when notice is and is not required for individual merchant banking investments.

The final rule also adds a new exception at § 225.87(b)(2) to the general post-transaction notice requirement. This new section provides that a FHC that has submitted a post-transaction notice in connection with a particular financial activity is not required to submit an additional notice under this section to commence the activity *de novo* through any other authorized subsidiary of the FHC without providing additional notice under § 225.87(a).[16] This exception applies only if the FHC already controls the company through which the activity will be commenced, and, thus, the acquisition by a FHC of control of a company engaged in a listed activity does not qualify for this exception. In addition, this new exception is not available if the Board, in the exercise of its supervisory authority, informs the FHC that notice is required for the commencement *de novo* of a financial activity.

Section 225.88—How To Request the Board To Determine That an Activity Is Financial in Nature or Incidental to a Financial Activity?

Under the GLB Act, the Board, in consultation with the Secretary of the Treasury, may expand the list of activities that are permissible for a FHC by determining that an additional activity is financial in nature or incidental to a financial activity. Section 225.88 permits a FHC or other interested party to request such a determination.

The rule provides that a request for a determination that an activity is financial in nature or incidental to a financial activity must identify and define the activity for which a determination is sought, explain in detail why the activity should be considered financial in nature or incidental, and provide information supporting the requested determination and any other information requested by the Board. The rule requires the Board to provide the Secretary of the Treasury a copy of the request and consult with the Secretary in accordance with section 4(k)(4)(2) of the BHC Act. The rule also allows the Board, after consultation with the Secretary, to publish a description of the proposal in the **Federal Register** with a request for public comment. The Board will attempt to make a final decision on a request filed under § 225.88 within 60 days of completion of both the consultative process and the public comment period, if any.

Like the interim rule, § 225.88 of the final rule also allows a FHC to request an advisory opinion from the Board regarding the scope an activity already determined to be financial and listed in § 225.86. Such a request must be in writing and provide a detailed description of the activity, product, or service about which the company is inquiring, an explanation supporting an interpretation regarding the scope of the permissible financial activity, and any other information required by the Board. The Board will respond to a requester within 45 days of receiving a complete written request.

Several commenters suggested that the Board, without waiting for a specific request, evaluate whether an activity is financial in nature or incidental to a financial activity if another Federal banking agency has authorized or authorizes depository institutions under its supervision to conduct the activity. The GLB Act allows the Board at its own initiative to propose authorizing an additional activity. In this regard, the Board anticipates monitoring developments in the banking and financial services industries in order to identify new activities that might be considered financial in nature or incidental thereto. However, the Board does not believe it is appropriate to propose as financial in nature or incidental all activities that another Federal banking agency may have authorized. The standards the Board must consider when authorizing a financial activity under the GLB Act may differ from the standards governing the authorization of new activities under other Federal banking laws. In light of these differences, the requirement that the Board consult with the Secretary of the Treasury in connection with financial activities, and the potential impact of new activities on the depository institution subsidiaries of financial holding companies, the Board believes that it is important to evaluate each activity authorized by another Federal banking agency on a case-by-case basis before proposing that the financial holding companies be allowed to conduct the activity.

Section 225.89—How To Request Approval To Engage in an Activity That Is Complementary to a Financial Activity?

The Board has adopted without amendment § 225.89 as originally proposed. This section includes a procedure for a FHC to obtain the Board's prior approval to engage in activity that the company believes is complementary to a financial activity in which the company is engaged. Generally, such a request must identify the proposed complementary activity and specifically discuss how it would be conducted; identify the financial activity for which the proposed activity would be complementary and provide information to support why the proposed activity should be considered complementary to the identified financial activity; describe the scope and relative size of the proposed activity; discuss the risks that conducting the activity reasonably may be expected to post to the safety and soundness of the company's subsidiary depository institutions and the financial system generally; describe the potential adverse effects and potential public benefits that could result from conducting the activity; and provide any additional information requested by the Board.

In acting on a proposal to engage in a complementary activity, the Board will consider whether the activity is complementary to the identified financial activity, whether the proposed activity would pose a substantial risk to the safety or soundness of depository institutions or the financial system generally, and whether the proposal could be expected to produce benefits to the public that outweigh possible adverse effects. The Board will act on a request for prior approval to engage in a complementary activity within the

[16] One commenter stated that a FHC should be allowed to commence the same financial activity in different subsidiaries using different sources of authority. As discussed above, some activities are authorized by more than one source of authority. A FHC therefore may commence the same activity in different subsidiaries using different sources of authority in accordance with the procedures applicable to the chosen authority.

time period described at section 4(j) of the BHC Act.

Section 225.90—What Are the Requirements for a Foreign Bank To Be Treated as a Financial Holding Company?

A foreign bank that is a bank holding company because it owns a subsidiary bank in the United States must comply with the same requirements as any other bank holding company that elects to be a financial holding company under the GLB Act. Most foreign banks, however, do not own subsidiary banks in the United States; instead, they operate U.S. branches that are part of the foreign bank itself.[17] Such foreign banks may, like U.S. bank holding companies, also elect to be treated as financial holding companies and thereby be able to engage in the new financial activities. For purposes of a foreign bank with a U.S. branch qualifying to be treated as a FHC, the Act requires the Board to apply capital and management standards to the foreign bank that are comparable to the standards applied to a U.S. bank owned by a FHC, giving due regard to the principle of national treatment and equality of competitive opportunity.

Well Capitalized Standards

Under the interim rule, a foreign bank with a U.S. branch could be considered well capitalized if either: (i) Its home country supervisor had adopted capital standards consistent with the Basel Capital Accord, the foreign bank maintained capital ratios generally equivalent to those required for a well capitalized U.S. bank (Tier 1 capital to total risk-based assets ratio of 6 percent and total capital to total risk-based assets ratio of 10 percent and a Tier 1 capital to total assets leverage ratio of at least 3 percent), and the Board determined that the foreign bank's capital was comparable to the capital required for a well capitalized U.S. bank; or (ii) the foreign bank had obtained a determination from the Board under § 225.91(c) that the bank's capital is otherwise comparable to the capital required of a well capitalized U.S. bank (the ''pre-clearance process'').

Most commenters criticized the use of a leverage ratio in assessing the capital of foreign banks. Some of the arguments made against imposing a leverage ratio on foreign banks were that: (i) It is contrary to the internationally accepted Basel Capital Accord and counterproductive to the work of the Basel Committee on Banking Supervision (the ''Basel Committee''); (ii) the imposition of a leverage ratio on foreign banks is inequitable due to the different composition of their balance sheets and the amount of nonbanking assets commonly held by foreign banks; and (iii) a leverage ratio requirement would require foreign banks to manage their worldwide capital accounts to meet a specific U.S. requirement, which is contrary to the principle of comprehensive consolidated home country supervision. One foreign bank supervisory authority, however, stated that it did not agree that the Basel Capital Accord was the only possible capital adequacy measure for a national regulator and could see how a Tier 1 leverage test could supplement the Basel Capital Accord in a meaningful way. Some domestic commenters expressed support for the imposition of a leverage ratio requirement on foreign bank FHCs. One commenter stated that requiring foreign banks to meet a leverage ratio of only 3 percent favors foreign institutions contrary to the provisions of the GLB Act and that, to ensure consistency, the lower capital requirement should be available to foreign banks only if they can demonstrate in their declaration and certification that they have implemented the market risk guidelines.

As the Board has previously noted, the numerical screening levels for capital are not the only determining factors in whether a foreign bank may be considered comparably capitalized. The pre-clearance process established by the interim rule allows a foreign bank that does not meet one or more of the screening levels to request a determination that it is nevertheless comparably well capitalized. Consequently, meeting the leverage ratio set out in the regulation has not been a prerequisite for FHC status, and a number of foreign banks have been found to meet FHC requirements despite not having met the leverage screening level.

The foreign bank FHC elections processed to date indicate that the application of a leverage ratio screen to non-U.S. banks may have limited value as a general rule in the assessment of comparability for FHC purposes because of the significant differences between U.S. and foreign banking balance sheets. The home country supervisors of most foreign banks do not require a bank to meet or manage toward any specific leverage ratio and generally do not take it into account in the consolidated supervision of the bank. In light of the comments received and the Board's experience to date in assessing foreign bank capital in FHC cases, the Board has determined to make several changes in the final regulation. The leverage ratio has been removed from the screening test in the definition of well capitalized in § 225.90(b)(1)(iii) in the final rule. The screening test will now reference a foreign bank's Tier 1 and total risk-based capital levels calculated under the Basel Accord. Accordingly, foreign banks from countries that follow Basel capital rules may submit declarations to be treated as FHCs without reference to any particular leverage ratio. For those countries that do not follow the Basel Accord, capital will continue to be assessed in the pre-clearance process.

The Board also believes, however, review of a non-U.S. bank's leverage ratio in particular cases may serve as an indicator that the bank's capital should receive further scrutiny in determining whether the bank has capital comparable to a well capitalized U.S. bank. Consequently, a foreign bank's leverage ratio will be considered by the Board as one of the factors that can be taken into account for purposes of the comparability review under § 225.92(e) and has been added to the list of factors in that section. Under this approach, the Board may consider whether the level of a foreign bank's leverage ratio is such that it indicates that additional analysis should be undertaken in assessing comparability.[18] Such assessments would in all cases be based on all relevant factors, and not merely on the leverage ratio. Thus, the Board would retain any benefits associated with reviewing the leverage ratio, but the foreign bank's qualification for FHC status would not be dependent upon it. Instead, qualification would depend on the overall capital strength of the foreign bank.

The Board intends that such reviews would be carried out within the 31-day processing period in cases where a certification has been filed and as expeditiously as possible in other cases. The Board also expects that staff would consult with the foreign bank's home country supervisor on issues relating to capital.

Well Managed Standards

Under the interim rule, a foreign bank was considered well managed if: (i) Each of the foreign bank's U.S. offices had received at least a satisfactory

[17] A foreign bank that operates a branch, agency, or commercial lending company subsidiary in the United States is subject to the BHC Act as if it were a bank holding company. In this portion of the preamble, the term ''branch'' is used to include all three of these forms of operation unless otherwise noted.

[18] The financial information necessary for System staff to compute a foreign bank's leverage ratio will be required as part of the certification process and ongoing reporting required of foreign FHCs.

composite rating at its most recent assessment; (ii) the foreign bank's home country supervisor considered the overall operations of the foreign bank to be satisfactory or better; and (iii) the management of the foreign bank met standards comparable to those required of a well managed U.S. bank.

Several commenters criticized the interim rule's requirement that each individual U.S. office of a foreign bank must have received at least a satisfactory composite rating at its most recent assessment in order for the foreign bank to certify that it is well managed. Some commenters argued that branches and agencies are not properly equated to domestic bank subsidiaries because many are small offices that do not function as independent financial institutions, but rather as marketing or relationship outposts of large, centralized regional headquarters. In addition, some commenters argued that a problem in one such office that can affect the rating of that office may, in fact, have an insignificant impact on the FBO's consolidated banking operations in the United States. Moreover, some commenters have noted that a U.S. bank may have a single branch in less than satisfactory condition and still be given a satisfactory rating overall.

In the final rule, the Board has revised this provision to require that each foreign bank be evaluated on the basis of a composite rating of all of its direct U.S. banking offices, while continuing to evaluate each U.S. depository institution subsidiary of the foreign bank separately. Although the Federal Reserve has traditionally tracked each branch or agency of a foreign bank as a separate entity, in order to make a comparison between U.S. and foreign banks for purposes of the FHC election, the Board has determined that each foreign bank should be evaluated for FHC purposes on the basis of a consolidated rating of all of its direct U.S. banking operations. Thus, in order to achieve comparable treatment, the well managed standard applicable to foreign bank FHCs has been revised in the final rule to require that a foreign bank have a satisfactory rating for its U.S. branches, agencies, and commercial lending company subsidiaries on a composite basis.

The Federal Reserve's foreign bank examination process has been amended to include assignment of a combined assessment of a foreign banking organization's U.S. branch, agency, and commercial lending company operations through the regular examination cycle.[19] Until this amendment is applied throughout the regular examination cycle, such combined U.S. banking assessments will be determined by the Board on a case by case basis based on the most recent individual office ratings. If a foreign bank that wishes to obtain FHC status has not been assigned a combined U.S. banking assessment as part of the regular examination cycle, the foreign bank should contact its responsible Federal Reserve Bank or utilize the pre-clearance process. A combined U.S. banking assessment may be assigned to a foreign bank as part of the FHC pre-clearance process. If a foreign banking group contains more than one foreign bank with U.S. banking offices, each such foreign bank in the group must have a satisfactory combined U.S. banking assessment in order for the foreign banking group or any of its subsidiaries to obtain FHC status.[20]

Several commenters also criticized the interim rule's requirement that the foreign bank's home country supervisor consider the overall operations of the foreign bank to be satisfactory or better. Commenters claimed that this requirement was vague, provided very little guidance to the home country supervisors, and would result in unwarranted delays and expense in FHC processing. Some commenters also claimed that this requirement was an extra-territorial expansion of the Board's jurisdiction and the Board, as a host country supervisor, should not require a foreign bank to satisfy a U.S. management standard in its operations outside the United States. Some commenters also incorrectly interpreted this provision as requiring a foreign bank's home country supervisors to evaluate the bank's global management according to the U.S. regulatory definition of ''satisfactory.''

The final rule amends this requirement to clarify that a foreign bank's home country supervisor must confirm that it consents to the proposed expansion of the foreign bank's U.S. operations. This formulation is based on guidelines issued by the Basel Committee. The Basel Committee has recognized the need for host country supervisors to seek the views of the home country supervisor prior to issuing a license to a foreign bank for new business in the host country. In its Core Principles for Effective Banking Supervision, the Basel Committee indicates that a key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved and that this contact ''should commence at the authorisation stage when the host supervisor should seek the approval from the home supervisor before issuing a license.[21] Moreover, the Basel Committee has indicated that a host country supervisor should consent to expansion of a foreign banking organization's activities within its jurisdiction only after the home country supervisor has given its consent to the expansion.[22] The final rule's requirement that the home country supervisor consent to the foreign bank's expansion of its U.S. operations under the GLB Act is well within the parameters of these guidelines. In accordance with Basel Committee guidelines, the home country supervisor should consider the foreign banking organization's consolidated capital and management before providing its consent to the expansion. In those situations in which there is no formal consent process in the home country, the Board will consult with the home country supervisor to assure itself that the supervisor considers the capital and management of the bank to satisfy its home country standards and that the supervisor has no objections to the expansion.

[19] See SR Letter No. 00–14 (SUP) (Oct. 23, 2000). The ''combined ROCA rating'' encompasses a foreign bank's U.S. branches, agencies, and commercial lending companies, but not its U.S. nonbanking subsidiaries. The combined ROCA rating will be factored into the foreign banking organization's overall Combined U.S. Operations Rating, which will continue to be a single composite rating that reflects the U.S. supervisors' collective assessment of all operations (*i.e.*, banking and nonbanking) of the foreign banking organization in the United States.

[20] Each U.S. depository institution subsidiary of a foreign bank would continue to be required to meet the well capitalized and well managed standards on an individual basis for the foreign bank or company to obtain FHC status in the same manner as required for U.S. bank holding companies.

[21] The Core Principles also indicate that the home country supervisor's responsibility extends to a bank's foreign subsidiaries as well as its branches, and supervisors should determine that a bank has the expertise needed to conduct its foreign activities, which may be fundamentally different from the bank's domestic operations, in a safe and sound manner. Basel Committee on Banking Supervision, ''Core Principles for Effective Banking Supervision'' pp. 40–41 (1997).

[22] Basel Committee on Banking Supervision, ''Minimum Standards for the Supervision of International Banking Groups and Their Cross-Border Establishments'' § II.2 (1992). In reviewing proposals for inward and outward expansion, the Basel Committee states that host country and home country authorities should, at a minimum, give weight to (a) the strength of the bank's and banking group's capital and (b) the appropriateness of the bank's and banking group's organization and operating procedures for the effective management of risks on a local and consolidated basis respectively.

Comparability of Capital and Management

In order for a foreign bank to qualify as a FHC under the interim rule, the Board must make affirmative findings that the foreign bank's capital and management are comparable to that required for a U.S. bank owned by a FHC. The interim rule lists discretionary factors that the Board may take into account in making this determination, such as the composition of capital, accounting standards, long-term debt ratings, reliance on government support to meet capital requirements, and the extent to which the foreign bank is subject to comprehensive consolidated supervision by its home country supervisor.

Some commenters objected to the inclusion of a Board comparability determination in the definitions of well capitalized and well managed, claiming that it is too vague and provides too much discretion to the Board. They also argue that the range of factors that can be taken into account in the comparability analysis and the required consultation with home country supervisors will significantly increase the likelihood that the 31-day processing period will be extended in the case of foreign banks. Some commenters argue that the final rule should not retain the Board's right to reject foreign banks' FHC elections if they fulfill the required capital ratios as calculated under the home country standard that is consistent with the Basel Capital Accord.

The final rule essentially retains the provisions contained in the interim rule that relate to the factors the Board may consider in making a comparability finding. The Board does not believe that these factors are either vague or overbroad. Rather, they are factors that allow a decision on comparability of capital and management to be made. All U.S. banks are subject to essentially the same regulatory framework, which includes frequent examinations and extensive quarterly reporting. Foreign banks, on the other hand, operate under supervisory and accounting systems that can differ significantly from U.S. systems and do not (and should not) report to U.S. authorities as extensively as U.S. banks. Under these circumstances, it is reasonable for the Board to retain the ability to evaluate these differences in deciding whether a foreign bank's capital and management meet the requirements of the FHC regulations.

One commenter specifically questioned whether the Board should take into account a foreign bank's reliance on government support to meet capital requirements in determining whether the foreign bank is well capitalized. The commenter argued that the Basel Capital Accord does not consider this factor in determining capital adequacy. The final rule retains this factor in the list of factors for determinations of capital and management comparability. In order to assure equality of competitive opportunity with U.S. banking organizations, the Board must be able to consider the impact of any assistance a foreign banking organizations receives from its home country for purposes of meeting capital requirements.

Comprehensive Consolidated Supervision

The interim rule included the ''extent to which'' a foreign bank is subject to comprehensive supervision on a consolidated basis by its home country supervisor in the list of factors the Board may take into account in determining whether a foreign bank is well capitalized and well managed. The interim rule also stated that a foreign bank chartered in a country where no other bank from that country has been reviewed by the Board for comprehensive consolidated supervision under the BHC Act or the International Banking Act is encouraged to use the pre-clearance process.

In the preamble to the January 19, 2000, interim rule, the Board stated that it expects that most foreign banks that elect to be treated as financial holding companies will be subject to comprehensive consolidated supervision, and that an election by a foreign bank that is not subject to comprehensive consolidated supervision will receive a more detailed review. The preamble to the Board's March 15, 2000, amendments to the interim rule specifically requested public comment on whether a foreign bank should be required to be subject to comprehensive consolidated supervision in order to obtain FHC status.

Two commenters addressed whether the final rule should include a comprehensive consolidated supervision requirement for foreign banks to obtain FHC status. One commenter argued that a foreign bank's eligibility to be treated as a FHC should not be conditioned on a comprehensive consolidated supervision standard. The commenter recognized, however, that it may be appropriate for the Board, when warranted by the circumstances of a particular case, to take into account the extent to which a foreign bank with a U.S. branch or agency is subject to comprehensive consolidated supervision as a factor that is relevant to its determination of whether the bank is well capitalized and well managed for purposes of the GLB Act. Another commenter encouraged the Board to require foreign banks to meet a comprehensive consolidated supervision standard, or follow the pre-clearance process, as a means of insuring that the foreign banks meet standards comparable to those required of U.S. banks.

The Board believes that, as a general rule, the top tier foreign bank in a foreign banking group should be subject to comprehensive consolidated supervision by its home country supervisor in order for the foreign banking group to obtain FHC status.[23] The fact that a foreign bank is subject to comprehensive consolidated supervision provides a host country supervisor, such as the Board for foreign FHCs, with a higher level of confidence that the capital and management information being submitted by the applicant is accurate and reliable.[24] Accordingly, the final rule adopts the position that, as a general matter, a foreign bank may not be considered to be well capitalized and well managed if the foreign bank is not subject to comprehensive consolidated supervision. The pre-clearance provision has been amended to clarify that a foreign bank that has not been determined to be subject to comprehensive consolidated supervision by the Board, and is chartered in a country where no other bank from that country has been determined by the Board to be subject to comprehensive consolidated supervision, is required (not merely encouraged) to use the pre-clearance process, even if it otherwise meets the objective screening criteria. The Board may review the home country supervision of a foreign bank through the pre-clearance process and make a

[23] Assuming that a top tier foreign bank in a foreign banking group is determined to be subject to comprehensive consolidated supervision, subsidiary foreign banks of the group should be incorporated into the supervisory framework of the home country supervisor of the top tier foreign bank and, thus, should be subject to comprehensive consolidated supervision even if the subsidiary foreign bank is not subject to comprehensive consolidated supervision by its own home country supervisor.

[24] The Basel Committee has stated that, as part of comprehensive consolidated supervision, a bank's home country supervisor should confirm to its own satisfaction the reliability of the consolidated financial and prudential information supplied by the bank on its global operations. Basel Committee on Banking Supervision, ''Minimum Standards for the Supervision of International Banking Groups and Their Cross-Border Establishments'' § II(1) (1992).

comprehensive consolidated supervision determination in that context. If the Board makes an affirmative comprehensive consolidated supervision determination through the FHC pre-clearance process, the determination will be relied upon for the foreign bank to establish additional branches and agencies under the Foreign Bank Supervision Enhancement Act.

The Board also believes, however, that there may be limited situations in which an exceptionally strong bank from a country that has not yet fully implemented comprehensive consolidated supervision should be able to be considered for FHC status. Accordingly, the regulation has been revised to allow a foreign bank that cannot be determined to be subject fully to comprehensive consolidated supervision to qualify for FHC status if certain factors are present. Such factors are: (i) That the home country supervisor has made significant progress in adopting and implementing arrangements for the consolidated supervision of its banks; and (ii) the foreign bank itself demonstrates significant financial strength, such as through high levels of capital or exceptional asset quality. A foreign bank that is not subject to comprehensive consolidated supervision may use the pre-clearance process to explain to the Board why it should be granted FHC status even in the absence of the supporting comprehensive consolidated supervision framework. The Board, however, anticipates granting FHC status to foreign banks that are not subject to comprehensive consolidated supervision only in rare instances.

Section 225.91—How May a Foreign Bank Elect To Be Treated as a Financial Holding Company?

Section 225.91 sets out the procedures to be followed by a foreign bank that operates a U.S. branch, or a company that owns or controls such a foreign bank in order to elect to be treated as a FHC. In order to be treated as a FHC, a foreign bank must file a written declaration with the appropriate Federal Reserve Bank. Generally, the declaration must: (i) State that the foreign bank or company elects to be treated as a FHC; (ii) provide the appropriate capital information on the foreign bank, any foreign bank that maintains a U.S. branch and is controlled by the foreign bank or company certificant, and any U.S. depository institution subsidiary of the foreign bank or company certificant; (iii) certify that the foreign bank, any foreign bank that maintains a U.S. branch and is controlled by the foreign bank or company certificant, and all U.S. depository institutions controlled by the foreign bank or company certificant are well capitalized and well managed as of the date the foreign bank or company files its election. This provision also provides for a pre-clearance process whereby a foreign bank or company may request a review of its qualifications to be treated as a FHC for the purposes of making the required certifications in the declaration prior to submitting its declaration.

The interim rule required that all foreign banks with direct U.S. operations that are controlled by a foreign bank or company seeking FHC status be well capitalized and well managed in order for the foreign banking group to be treated as a FHC. Commenters raised two distinct issues regarding this requirement. As an initial issue, some commenters suggested that a foreign bank with a U.S. branch that is controlled by another foreign bank should not be required to meet the well capitalized and well managed standards if the controlling foreign bank does not intend for the subsidiary foreign bank to exercise any of the expanded powers authorized by the GLB Act. One commenter stated that, if a foreign bank FHC has a subsidiary foreign bank, but the subsidiary foreign bank does not intend to engage in the expanded FHC activities in the United States, the GLB Act does not require that the subsidiary foreign bank be made subject to the capital and management standards. The commenter suggested that the Board should assess the capital and management of the controlling foreign bank both separately and on a consolidated basis after taking account of the subsidiary foreign bank, but should not apply the well capitalized and well managed standards separately to such subsidiary foreign bank.

The final rule retains the requirement that each foreign bank that maintains a U.S. branch and is controlled by a foreign bank or company electing to be treated as a FHC must meet capital and management standards comparable to those required of U.S. banks owned by FHCs. Under the GLB Act, all of the depository institution subsidiaries of a bank holding company must be well capitalized and well managed in order for the bank holding company to qualify for FHC status, regardless of where in the corporate structure the expanded activities are to be located. Permitting a foreign bank to evade a similar requirement merely by placing the expanded activities in a particular location in its organization could provide foreign banks with a competitive advantage over U.S. bank holding companies. If a foreign bank competes directly against U.S. banks in the U.S. banking market, the Board believes it should meet capital and management standards comparable to the standards applied to U.S. banks.

As a second issue, some commenters claim that this requirement could greatly impact the ability of a foreign bank electing FHC status to align itself with other non-U.S. banks through strategic minority investments of greater than 25 percent of voting shares. Commenters argue that the electing foreign bank or company can have statutory ''control'' over another foreign bank for purposes of U.S. banking law when the electing foreign bank does not have majority control over the other foreign bank. If the other foreign bank does not meet the well capitalized and well managed standards, the electing foreign bank may not have the ability to direct the other foreign bank to improve its capital and management in order to meet the FHC standards or, alternatively, to close or divest its U.S. offices. In such instance, the electing foreign bank would be required to either divest its investment in the other foreign bank or forgo the opportunity to engage in the expanded activities in the United States.

The final rule retains as a general rule the requirement that each foreign bank within a banking group that maintains U.S. offices must meet the comparable capital and management standards. There may be limited situations involving strategic minority investments between foreign banks where some relief from this requirement may be justified. A foreign bank or company in this type of situation may utilize the pre-clearance process to request a determination that it should not be held accountable for another foreign bank with U.S. offices that does not meet the capital and management standards. The Board anticipates, however, that any relief from this requirement would be granted only in limited circumstances where the foreign bank can clearly demonstrate that it has no ability to control the other foreign bank.

Section 225.92—How Does an Election by a Foreign Bank Become Effective?

Section 225.92 describes the procedures and timing under which a foreign bank's FHC election will be effective and the situations under which the Board will find that the election is ineffective. Generally, an election will be effective on the 31st day after the date the election was received by the appropriate Federal Reserve Bank, unless the Board notifies the foreign bank or company prior to that time that

the Board has found that the election is ineffective or the period is extended with the consent of the foreign bank or company. The election may become effective prior to the 31st day after the date it was received if the foreign bank or company is so notified by the Board or the appropriate Federal Reserve Bank.

An election may be found by the Board to be ineffective if the Board finds that the foreign bank electing FHC status, any other foreign bank with U.S. offices that is controlled by the foreign bank or company electing FHC status, or any U.S. depository institution controlled by the electing foreign bank or company does not meet the applicable standards for capital or management. In addition, the Board may find an election ineffective if the Board determines that it does not have sufficient information to assess whether the foreign bank or company making the election meets the requirements of this subpart.

Some commenters criticized the processing provisions of the interim rule. As it was initially issued on January 19, 2000, § 225.92 stated that an election filed by a foreign bank or company would not be effective until the Board made an affirmative finding that the foreign bank was well capitalized and well managed. In its March 15, 2000, amendments to the interim rule, based on the Board's experience in reviewing and acting on foreign bank FHC elections during that period and to accommodate concerns expressed by commenters regarding the difference in process applicable to foreign banks, the Board revised the processing provision to make an election filed by a foreign bank that met the interim rule's quantitative capital requirements and the well managed standards effective on the 31st day after filing. The interim rule was amended at that time, however, to allow the Board to find an election ineffective if the Board did not have sufficient information to assess whether the foreign bank meets the capital and management standards.

One commenter argued that the separate election processing track for foreign banks may be in conflict with the Board's longstanding principle of providing national treatment for foreign banks. The commenter also claimed that the likelihood that the 31-day processing period for foreign banks will be extended is significantly increased because of the range of factors that the Board may, in its discretion, evaluate with respect to foreign banks and that this additional discretion also may cause the Board to determine that it does not have sufficient information to declare the FHC election effective. Another commenter argued that if a foreign bank certified that it met the applicable capital and management standards in its FHC election, it must be permitted to engage in expanded financial activities on the 31st day after the date the election is received.

The final rule retains the processing provision in the amended interim rule. The Board has found that this provision does not lead to delays in dealing with certifications filed by foreign banks, all of which have been processed within 31 days. Similarly, a number of pre-clearance requests have been processed in the same time frame. The Board notes that it has ready access to all relevant information for U.S. banks and, thus, is assured of being able to make the appropriate judgments within the statutory timeframes. The Board does not similarly have ready access to all relevant information for foreign banks. The GLB Act requires the Board to apply comparable capital and management standards to foreign banks. There may be situations where foreign banks must submit additional information in order for the Board to be able to make a judgment on the qualifications of the foreign bank under the regulation. The limited discretion provided by the processing provisions of the final rule should ensure that the Board is not forced to deny a FHC election of a foreign bank because the foreign bank has not supplied additional information requested by the Board on a timely basis.[25]

Section 225.93—What Are the Consequences of a Foreign Bank Failing To Continue To Meet Applicable Capital and Management Requirements?

Section 225.93 establishes the procedures to be followed when the Board finds that a foreign bank FHC no longer complies with the FHC standards. This section parallels § 225.83, with appropriate modifications. It sets out the procedures to be followed in the event that a foreign bank that is treated as a FHC ceases to meet the applicable capital and management requirements. It provides for the execution of an agreement designed to bring the foreign bank or company back into compliance with the requirements of the regulation and permits the Board to impose certain limitations on the U.S. activities of such a foreign bank or company during any period of noncompliance. Finally, the section sets forth the consequences of a failure to correct the noncompliance within a period of 180 days. Such consequences could include termination of the foreign bank's U.S. branches and agencies and divestiture of its commercial lending company subsidiaries or ceasing to engage in the expanded activities permitted for financial holding companies.

The interim rule stated that, in taking any action under this provision, the Board would consult with the relevant Federal and state regulatory authorities. Some commenters noted that the section did not also expressly state that the Board would consult with the foreign bank's home country supervisor. Several commenters argued that consultations between the Board and the foreign banks' home country supervisors must take place in the case of non-compliance of a foreign bank with the FHC requirements. One commenter also stated that the interim rule's section provides for the active intervention of the Board in the management of the parent company of a foreign FHC which ceases to meet applicable capital and management standards and this authority harbors potentially serious extra-territorial implications.

As the U.S. supervisor responsible for the operations of foreign banks in the United States and of FHCs generally, the Board has supervisory responsibility to ensure that foreign banks and companies treated as FHCs engage in the expanded activities permitted by the GLB Act in the United States in a safe and sound manner.[26] This section relates only to the U.S. activities of a foreign bank or company FHC and does not involve extra-territorial extension of the Board's authority as host country supervisor. In accordance with Basel Committee guidelines, the Board generally informs a foreign bank's home country supervisor regarding any area of the foreign bank's U.S. business that raises a significant level of supervisory concern for the Board, including whether the foreign bank or its affiliates are in compliance with U.S. law and

[25] The Basel Committee has recognized the need for a banking authority to have the right to reject a license application ''if it cannot be satisfied that the criteria set are met.'' Basel Committee on Banking Supervision, ''Core Principles for Effective Banking Supervision'' p.16 (1997).

[26] Under the IBA, the Board has the authority to take supervisory action against the U.S. offices of foreign bank if the Board determines that the foreign bank, or any affiliate of the foreign bank, has committed a violation of law or engaged in any unsafe or unsound banking practice in the United States. 12 U.S.C. 3105(e). In addition, the IBA expressly makes foreign banks with U.S. branches subject to the provisions of the BHC Act in the same manner and to the same extent that bank holding companies are subject to such provisions. 12 U.S.C. 3106(a).

regulation.[27] For the avoidance of doubt, the final rule expressly states that the Board will consult with the relevant home country supervisor of a foreign bank in taking any action under this section.

The final rule also adopts provisions that generally parallel the amendments made to § 225.83 with respect to triggering events for notifying the Board that the foreign bank has ceased to be well capitalized or well managed under the regulation.

Regulatory Flexibility Act

The Board has reviewed the final rule in accordance with the Regulatory Flexibility Act. This final rule implements provisions of Title I of the Gramm-Leach-Bliley Act that allow entities that qualify as FHCs to engage in a broad range of securities, insurance, and other financial activities by providing the Board with a simple, post-transaction notice. The rule should enable bank holding companies and foreign banks that qualify as financial holding companies to engage in an expanded range of activities by, in most cases, submitting a simple form to the appropriate Federal Reserve Bank describing the relevant activity.

The FHC election procedures described in this rule are voluntary, and the criteria set forth in the rule for an effective election filing are those established by the GLB Act. The rule implements this part of the GLB Act by requiring a simple, one-time procedure involving minimum paperwork to fulfill the statutory election requirement. In addition, the new powers described in the GLB Act and implemented by this rule should enhance the overall efficiency of bank holding companies and the other financial companies that seek to affiliate with them. The rule applies to all companies that attempt to qualify as financial holding companies, regardless of their size, and allows small organizations to take advantage of the broad new powers conferred by the GLB Act with minimal additional burden.

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR part 1320 Appendix A.1), the Board reviewed the rule under the authority delegated to the Board by the Office of Management and Budget. The Federal Reserve may not conduct or sponsor, and an organization is not required to respond to, this information collection unless it displays a currently valid OMB control number. The OMB control number is 7100–0292.

The collection of information requirements in this final rulemaking are found in 12 CFR 225.82 (a) and (b), 225.83 (b) and (c), 225.91 (a), 225.93 (b) and (c); and 225.87, 225.88, and 225.89. This information is required to evidence compliance with the requirements of Title I of the Gramm-Leach-Bliley Act (Pub. L. 106–103, 113 Stat. 1338 (1999)) which amends section 4 of the Bank Holding Company Act (12 U.S.C. 1843). The respondents are current and future bank holding companies and foreign banking organizations; and financial holding companies, respectively.

The notice cited in 12 CFR 225.82(a) provides that a bank holding company may elect to become a financial holding company by filing a simple written declaration with the Federal Reserve. The declaration must include information identifying the company's subsidiary depository institutions and their capital ratios, and a certification that each depository institution is well capitalized and well managed (for specific details, see 12 CFR 225.82 (b)). There will be no reporting form for this information collection. The agency form number for this declaration will be the FR 4010. The Board estimates that approximately 500 bank holding companies will file this declaration during the first year and that it will take approximately 15 minutes to complete this information. This would result in estimated annual burden of 125 hours. Based on a rate of $20 per hour, the annual cost to the public for this information collection is estimated to be $2,500.

The notice cited in 12 CFR 225.91(a) provides that 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. The declaration must state that they intend to be treated as an FHC; include their risk-based capital ratios, amount of Tier 1 capital, and total assets; certify that they are well capitalized and well managed; certify that all U.S. depository institution subsidiaries of the foreign bank or company are well capitalized and well managed; and provide the capital ratios for each U.S. depository institution subsidiaries of the foreign bank or company (for specific details, see 12 CFR 225.91(b)). There will be no reporting form for this information collection. The agency form number for this declaration will be the FR 4010. The Board estimates that approximately 15 foreign banks will file this declaration during the first year and that it will take approximately 30 minutes to complete this information. This would result in estimated annual burden of 7.5 hours. Based on a rate of $20 per hour, the annual cost to the public for this information collection is estimated to be $150.

The notice cited in 12 CFR 225.83(b) provides that a financial holding company with subsidiary depository institutions that cease to be well managed or capitalized, must notify the Federal Reserve and execute an agreement acceptable to the Federal Reserve within 45 days. Similarly, the notice cited in 12 CFR 225.93(b) provides that if a 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 that cease to be well capitalized or well managed, the foreign bank or parent company must notify the Federal Reserve and execute an agreement acceptable to the Federal Reserve within 45 days. If the financial holding company or foreign bank would like to request additional time they must provide an explanation of why an extension is necessary. For specific details about what should be included in this agreement, see 12 CFR 225.83(c)(3) and 225.93(c)(3), respectively. There will be no reporting form for this information collection. The agency form number will be the FR 4012. The Federal Reserve estimates that due to the new incentives, only 10 subsidiary depository institutions of financial holding companies and only 1 subsidiary of a foreign bank will fall into this category per year and that it would take approximately 10 hours to complete this information. This would result in estimated annual burden of 110 hours. Based on a rate of $20 per hour, the annual cost to the public for this information collection would be $2,200.

The post-transaction notice cited in 12 CFR 225.87(a) provides that 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 Federal Reserve Bank in writing within 30 calendar days. See 12 CFR 225.87(a) for specific details on the content of the notice. There are reporting forms for this information collection. For domestic FHCs, this form is the FR Y–6A (OMB No. 7100–0124) and for foreign FHCs, the form is the FR Y–7A (OMB No. 7100–0125). 65 FR 20821 (April 18, 2000). These forms

[27] Working group of the Basel Committee on Banking Supervision and the Offshore Group of Banking Supervisors, ''The Supervision of Cross-Border Banking'' section III(b) ¶ 14 (Oct. 1996).

shortly will be replaced by the FR Y–10 and FR Y–10F (OMB No. 7100–0297), respectively.

The Federal Reserve estimates that financial holding companies will make 450 filings of this notice annually and that it would take approximately 1 hour to complete this notification. This would result in an estimated annual burden of 450 hours. Based on a rate of $20 per hour, the annual cost to the public for this information collection would be $9,000.

Financial holding companies requesting the Board's determination that an activity is financial in nature or incidental to a financial activity must provide to the Board the information described in 12 CFR 225.88(b). Financial holding companies may request an advisory opinion from the Board about whether a specific proposed activity falls within the scope of an activity listed in 12 CFR 225.86 as financial in nature or incidental to a financial activity by submitting the information described in 12 CFR 225.88(e). Financial holding companies that seek prior approval to engage in an activity that the financial holding company believes is complementary to a financial activity must provide to the Board the information identified in 12 CFR 225.89(a). The Federal Reserve estimates that only 25 financial holding companies would file the information requested in these sections annually and that it would take approximately 1 hour to complete each information collection. This would result in estimated annual burden of 25 hours. Based on a rate of $20 per hour, the annual cost to the public for this information collection would be $500.

A bank holding company may request confidentiality for the information contained in these information collections pursuant to section (b)(4) and (b)(6) of the Freedom of Information Act (5 U.S.C. 552(b)(4) and (b)(6)).

The Federal Reserve has a continuing interest in the public's opinions of our collections of information. At any time, comments regarding the burden estimate, or any other aspect of this collection of information, including suggestions for reducing the burden, may be sent to: Secretary, Board of Governors of the Federal Reserve System, 20th and C Streets, NW., Washington, DC 20551; and to the Office of Management and Budget, Paperwork Reduction Project (7100–0292), Washington, DC 20503.

List of Subjects in 12 CFR Part 225

Administrative practice and procedure, Banks, Banking, Federal Reserve System, Holding companies, Reporting and recordkeeping requirements, Securities.

For the reasons set out in the preamble, the Board amends 12 CFR part 225 as follows:

PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL (REGULATION Y)

1. The authority citation for part 225 is amended to read as follows:

Authority: 12 U.S.C. 1817(j)(13), 1818, 1828(o), 1831i, 1831p–1, 1843(c)(8), 1843(k), 1844(b), 1972(l), 2903, 2905, 3106, 3108, 3310, 3331–3351, 3907, and 3909.

2. In subpart A, § 225.1, a new paragraph (c)(9) is added to read as follows:

§ 225.1 Authority, purpose, and scope.

* * * * *

(c) * * *

(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.

* * * * *

3. In subpart A, § 225.2 is amended by revising paragraph (r)(2) and (s) and adding paragraph (t) to read as follows:

§ 225.2 Definitions

* * * * *

(r) * * *

(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.

* * * * *

(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:

(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)).

* * * * *

4. In subpart B, § 225.14(c)(2)(i) is revised to read as follows:

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

* * * * *

(c) * * *

(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;

* * * * *

5. In subpart C, § 225.23(c)(2)(i) is revised to read as follows:

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

* * * * *

(c) * * *

(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;

* * * * *

6. Subpart I is revised to read as follows:

Subpart I—Financial Holding Companies

Sec.

225.81 What is a financial holding company?
225.82 How does a bank holding company elect to become a financial holding company?
225.83 What are the consequences of failing to continue to meet applicable capital and management requirements?
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?
225.85 Is notice to or approval from the Board required prior to engaging in a financial activity?
225.86 What activities are permissible for any financial holding company?
225.87 Is notice to the Board required after engaging in a financial activity?
225.88 How to request the Board to determine that an activity is financial in nature or incidental to a financial activity?
225.89 How to request approval to engage in an activity that is complementary to a financial activity?
225.90 What are the requirements for a foreign bank to be treated as a financial holding company?
225.91 How may a foreign bank elect to be treated as a financial holding company?
225.92 How does an election by a foreign bank become effective?
225.93 What are the consequences of a foreign bank failing to continue to meet applicable capital and management requirements?
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?

Subpart I—Financial Holding Companies

§ 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)).

§ 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.

Dated: December 21, 2000.

By order of the Board of Governors of the Federal Reserve System.

Jennifer J. Johnson,

Secretary of the Board.

[FR Doc. 01–34 Filed 1–2–01; 8:45 am]

BILLING CODE 6210–01–P