

FEDERAL RESERVE BANK OF DALLAS
DALLAS, TEXAS 75222

Circular No. 72-284
December 15, 1972

PROPOSED AMENDMENT TO REGULATION Y

To All Banks and Others Concerned
in the Eleventh Federal Reserve District:

The Board of Governors of the Federal Reserve System invites comments on a revised proposal to permit bank holding companies to lease both real and personal property under substantially the same conditions. Comments are to be received through January 5, 1973.

If adopted, the proposal would supersede the existing regulatory provision authorizing bank holding companies to engage in personal property leasing, and would put leasing of both real and personal property under a common set of rules. This new proposal takes the place of a proposal published in Circular No. 72-40 on February 25, 1972 with the effective date of February 18, 1972, which was concerned with real property leasing only. The Board will consider the comments received following that proposal.

In announcing the proposal, the Board said:

"Permitting bank holding companies to act as agent, broker or adviser in connection with financial leases, as proposed to be authorized, would not give bank holding companies authority to act as general agents or brokers for real or personal property transactions not otherwise meeting the conditions set forth in this regulation. Although certain additional restrictions would, as a technical matter, be imposed on personal property leasing, they are not intended or expected to have any practical effect on personal property leasing of bank holding companies, as presently authorized by the Board."

The Board proposed that "leasing real and personal property or acting as agent, broker or adviser in leasing such property" be a permissible activity for bank holding companies, provided the following conditions are met:

1. The lease is to serve as the functional equivalent of an extension of credit to the lessee of the property;
2. The property to be leased is acquired specifically for the leasing transaction under consideration;

3. The lease is on a nonoperating basis;
4. At the inception of the initial lease the effect of the transaction (and, with respect to municipal corporations only, reasonably anticipated future transactions) will yield a return from (1) rentals, (2) estimated tax benefits (investment tax credit and tax deferral from accelerated depreciation) and (3) in the case of personal property, but not real property, the estimated salvage value at the end of the minimum useful life allowed by the Internal Revenue Service, that will compensate the lessor for not less than the lessor's full investment in the property plus the estimated total cost of financing the property over the term of the lease;
5. At the expiration of the lease all interest in the property shall be liquidated as soon as practicable but in no event later than two years from the expiration of the lease, and
6. The maximum term of the lease, including renewals, shall be no more than 30 years.

The proposal is one of a series the Board has made concerning activities regarded as closely related to banking under the 1970 Amendments to the Bank Holding Company Act of 1956, and thus permissible activities for bank holding companies, subject to Board approval in individual cases.

A copy of the proposal is attached.

Yours very truly,

P. E. Coldwell,

President

Attachment

FEDERAL RESERVE SYSTEM

[12 CFR Part 225]

[Reg. Y]

Nonbanking Activities of Bank Holding Companies

The Board of Governors has considered the comments received on its proposal (37 Federal Register 4098) to permit bank holding companies, under the authority of section 4(c)(8) of the Bank Holding Company Act, to engage in real property leasing under certain conditions. Upon further consideration of the regulatory proposal the Board believes it is desirable to have uniformity of regulation with regard to the leasing activities of bank holding companies. Accordingly, the Board proposes to amend section 225.4(a) of Regulation Y to permit bank holding companies, subject to the procedures of section 225.4(b), to engage in the leasing of both real and personal property under substantially the same conditions.

If the proposal is adopted, it would supersede the existing regulatory provision authorizing bank holding companies to engage in personal property leasing (12 CFR 225.4(a)(6)) and related interpretation (12 CFR 225.123(d)). Permitting bank holding companies to act as agent, broker or adviser in connection with financial leases, as proposed to be authorized, would not give bank holding companies authority to act as general agents or brokers for real or personal property transactions not otherwise meeting the conditions set forth in this regulation. Although certain additional restrictions would, as a technical matter, be imposed on personal property leasing, they are not intended or expected to have any practical effect on

personal property leasing operations of bank holding companies, as presently authorized by the Board. Furthermore, although the proposal would not permit the recognition of residual value for real property leased in computation of the lessor's "full pay-out" recovery, it is understood that such property might be sold at the expiration of the lease for a price that would produce some additional return to the lessor.

The text of the proposed amendment reads as follows:

§ 225.4--Nonbanking Activities.

(a) Activities closely related to banking or managing or controlling banks. * * * * * The following activities have been determined by the Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto:

(6) Leasing real and personal property or acting as agent, broker or adviser in leasing such property provided:

(i) the lease is to serve as the functional equivalent of an extension of credit to the lessee of the property;

(ii) the property to be leased is acquired specifically for the leasing transaction under consideration;

(iii) the lease is on a nonoperating basis;

(iv) at the inception of the initial lease the effect of the transaction (and, with respect to municipal corporations only,

reasonably anticipated future transactions*) will yield a return from (1) rentals, (2) estimated tax benefits (investment tax credit and tax deferral from accelerated depreciation) and (3) in the case of personal property, but not real property, the estimated salvage value at the end of the minimum useful life allowed by the Internal Revenue Service, that will compensate the lessor for not less than the lessor's full investment in the property plus the estimated total cost of financing the property over the term of the lease;**

(v) at the expiration of the lease all interest in the property shall be liquidated as soon as practicable but in no event later than two years from the expiration of the lease; and

(vi) the maximum term of the lease, including renewals, shall be no more than 30 years.

To aid in the consideration of this matter by the Board, interested persons are invited to submit relevant data, views, or argument. Any such material should be submitted in writing to the Secretary, Board of

* The Board understands that by law some municipal corporations may not enter into a lease for a period in excess of one year. Such an impediment does not prohibit a company authorized under § 225.4(a) from entering into a lease with the municipality if the company reasonably anticipates that the municipality will renew the lease annually until such time as the company is fully compensated for its investment in the leased property plus its costs of financing the property. Further, a company authorized under § 225.4(a) may also engage in a so-called "bridge" lease financing of personal property, but not real property, where the lease is short term pending completion of long term financing, by the same or another lender.

** The estimate by the lessor of the total cost of financing the property over the term of the lease should reflect, among other factors, the term of the lease, the modes of financing available to the lessor, the credit rating of the lessor and prevailing rates in the money and capital markets.

Governors of the Federal Reserve System, Washington, D. C. 20551, to be received not later than January 5, 1973. Such material will be made available for inspection and copying upon request except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information.

Board of Governors of the Federal Reserve System, December 5, 1972.

(Signed) Michael A. Greenspan

Michael A. Greenspan
Assistant Secretary of the Board

(SEAL)