

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 82-42
April 13, 1982

REGULATION Y
BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL ACT

(Final Rulemaking Relating to Nonbanking Activities)

TO ALL MEMBER BANKS,
BANK HOLDING COMPANIES
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

The Board of Governors of the Federal Reserve System has amended its Regulation Y by adding to the list of activities permissible to bank holding companies the provision of management consulting advice to unaffiliated nonbank depository institutions. The amendment also permits management interlocks, under certain conditions, between bank holding companies and depository institutions to which they provide management consulting. Comments on this ruling were requested by Circular No. 81-220, dated November 19, 1981.

Enclosed are copies of the Board's press release and the related notice as it appeared in the Federal Register. It is suggested that you retain this circular until the amendments are received for insertion in Vol. II of your Regulations Binders.

Any questions concerning this material may be directed to Robert D. Hankins of our Holding Company Supervision Department, Ext. 6120.

Additional copies of this circular will be furnished upon request to the Department of Communications, Financial and Community Affairs of this bank, Ext. 6289.

Sincerely yours,



William H. Wallace
First Vice President

Enclosure

FEDERAL RESERVE press release



For immediate release

March 11, 1982

The Federal Reserve Board today announced the adoption of an amendment to Regulation Y adding to the list of activities permissible to bank holding companies the provision of management consulting advice to unaffiliated nonbank depository institutions.

The Board acted after consideration of comment received on its proposal issued in October 1981, in connection with an application by BankAmerica Corporation.

Under the amendment, management consulting advice could be offered to institutions such as savings and loan associations, mutual savings banks and other types of depository institutions that are not commercial banks. Previously, the Board's rules permitted bank holding companies to provide management consulting advice only to commercial banks.

The amendment also permits management interlocks, under certain conditions, between bank holding companies and depository institutions to which they provide management consulting.

The Board's notice in this matter is attached.

FEDERAL RESERVE SYSTEM**12 CFR PART 225**

[Docket No. R-0369; Regulation Y]

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 is amending its Regulation Y to include in the list of permissible bank holding company activities the activity of offering management consulting advice to unaffiliated nonbank depository institutions. These institutions would include savings and loan associations, mutual savings banks, credit unions, industrial banks, Morris Plan banks, cooperative banks, and industrial loan companies. The permissible activities

would include, but not be limited to, the selling to nonaffiliated nonbank depository institutions of management consulting services which relate to bank operations and marketing, bank personnel operations, and consumer financial information. The Board also is amending Regulation Y to permit bank holding companies to have management interlocks with depository institutions to which they provide management consulting services if such interlocks would be permissible under exceptions contained in Regulation L that apply to institutions in need of management or operating expertise.

EFFECTIVE DATE: April 20, 1982.

FOR FURTHER INFORMATION CONTACT:

Melanie L. Fein, Attorney, (202) 452-3594, Legal Division, Board of Governors of the Federal Reserve System.

SUPPLEMENTARY INFORMATION: Section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1843(c)(8)) permits bank holding companies to hold shares of "any company the activities of which the Board, after due notice and opportunity for hearing, determines (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto." The Board's Regulation Y specifies activities that it has determined to be closely related to banking and thus permissible for bank holding companies under section 4(c)(8). (12 CFR 225.4(a)). In determining whether a particular activity is a proper incident to banking or managing or controlling banks, the Board is required to consider "whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices."

Section 225.4(a)(12) of Regulation Y permits bank holding companies to provide management consulting services to nonaffiliated banks. The Board has stated in a published interpretation that such activities should be provided "only to an institution that both accepts deposits that the depositor has a legal right to withdraw on demand and engages in the business of making commercial loans." 12 CFR 225.131. The Board has regarded this interpretation as excluding most thrift institutions.

In response to a request by a bank holding company for prior approval to offer management consulting services to nonaffiliated nonbank depository

added to Regulation L. These include exceptions for depository organizations controlled or managed by women or minorities, newly chartered organizations, and organizations facing conditions endangering safety or soundness or disruptive loss of management officials due to the prohibitions in Regulation L. 12 CFR 212.4(b). The exceptions may be granted by the appropriate federal supervisory agency in individual cases on the basis of a determination that the exception is necessary to provide management or operating expertise to the requesting institution. These Regulation L exceptions have not yet been incorporated into the Regulation Y provision that prohibits interlocks between bank holding companies and client institutions to which they provide management consulting services. The Board is incorporating them at this time since the public interest they serve in Regulation L would similarly be served by their inclusion in Regulation Y. The amendment in this regard uses the terminology of the Depository Institution Management Interlocks Act of 1978, 12 U.S.C. 3201 *et seq.*, which refers to interlocks by "management officials," instead of the language in section 8 of the Clayton Act, which was superseded by the Interlocks Act, which refers to "officer, director, or employee" interlocks.

Pursuant to section 605(b) of the Regulatory Flexibility Act (Pub. L. No. 96-354; 5 U.S.C. 601 *et seq.*), the Board of Governors of the Federal Reserve System certifies that the amendment will not have a significant economic impact on a substantial number of small entities that would be subject to the regulation. The amendment would liberalize the existing regulations and does not have any particular effect on small entities that would be subject thereto.

Accordingly, pursuant to its authority under section 5(b) of the Bank Holding Company Act, 12 U.S.C. 1844(b), the Board of Governors of the Federal Reserve System amends 12 CFR Part 225, as follows:

PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL

12 CFR Part 225 is amended as follows:

1. The authority citation for Part 225 reads as follows:

Authority. Sec. 5, 70 Stat. 137; 12 U.S.C. 1844, unless otherwise noted.

2. Section 225.4 is amended by

revising paragraph (a)(12) to read as follows:

§ 225.4 Nonbanking activities.

(a) * * *

(12) Providing management consulting advice ^{10c} to nonaffiliated bank and nonbank depository institutions, including commercial banks, savings and loan associations, mutual savings banks, credit unions, industrial banks, Morris Plan banks, cooperative banks, and industrial loan companies, *Provided* that,

(i) Neither the bank holding company nor any of its subsidiaries own or control, directly or indirectly, any equity securities in the client institution;

(ii) No management official, as defined in 12 CFR 212.2(h), of the bank holding company or any of its subsidiaries serves as a management official of the client institution except where such interlocking relationships are permitted pursuant to an exemption granted under 12 CFR 212.4(b);

(iii) The advice is rendered on an explicit fee basis without regard to correspondent balances maintained by the client institution at any depository institution subsidiary of the bank holding company; and

(iv) Disclosure is made to each potential client institution of (A) the names of all depository institutions which are affiliates of the consulting company, and (B) the names of all existing client institutions located in the same county(ies) or SMSA(s) as the client institution.¹¹

By order of the Board of Governors of the Federal Reserve System, March 11, 1982.

William W. Wiles,

Secretary of the Board.

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^{10c} In performing this activity, bank holding companies are not authorized to perform tasks or operations or provide services to client institutions either on a daily or continuing basis, except as shall be necessary to instruct the client institution on how to perform such services for itself. See also the Board's interpretation of bank management consulting advice (12 CFR 225.131). This interpretation shall apply to the performance of management consulting services for nonbank depository institutions as well as for commercial banks.

¹¹ A bank holding company that has received the Board's prior approval to engage in offering management consulting advice to nonaffiliated commercial banks as of April 20, 1982, may offer such advice to nonbank depository institutions pursuant to this paragraph without filing an application under section 4(c)(8) of the Bank Holding Company Act for prior approval to engage in the activity, provided that it does not acquire a going concern to provide such advice.

organizations, the Board on November 3, 1981 requested public comment on proposed rule to amend Regulation Y to specifically authorize the provision of such services to nonbank clients. The Board requested interested persons to comment on whether the provision of management consulting services to nonbank clients is "closely related to banking or managing or controlling banks" and whether the performance of such services to nonbank clients can "reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, conflicts of interests, or unsound banking practices." The Board also requested comment on a proposal to amend Regulation Y to permit bank holding companies to have management interlocks with depository institutions to which they provide management consulting services if such interlocks would be permissible under exceptions contained in Regulation L (12 CFR 212) that apply to institutions in need of management or operating expertise.

The Board received forty-nine comments favoring the proposal and three comments opposing it. The comments favoring the proposal asserted that the provision of management consulting services to nonbank depository institutions was closely related to banking since banks traditionally have provided such services to unaffiliated commercial banks. Many commenters asserted that banks in fact provide management consulting services to nonbank depository institutions through correspondent relationships.

The comments favoring the proposal stated that the proposed activity would offer public benefits by increasing the availability of management consulting advice to all depository institutions. These comments also stated that the proposal would produce procompetitive benefits by assisting thrift institutions to fully utilize the powers conferred by the Monetary Control Act.

On the basis of the comments received and the Board's consideration of this matter, the Board has determined that the proposed activity is closely related to banking. Banks traditionally have provided management consulting services to nonaffiliated commercial banks and thus have provided services that are functionally similar to the proposed service. Moreover, banks traditionally have provided specialized services to nonbank depository institutions that those institutions either

have been precluded by law from providing for themselves or which they did not have the capability to provide for themselves. National banks have been permitted to offer a wide range of consulting and advisory services to nonbank financial institutions for some time.

Accordingly, the Board has determined that it would be appropriate to amend Regulation Y to include the activity on the list of permissible bank holding company activities. In order to guard against possible adverse effects of the proposal, such as the possibility for anticompetitive cooperative arrangements, improper use of confidential information, and similar abuses, the Board has determined that the provision of management consulting advice to nonbank clients should be subject to the same restrictions that apply when such services are provided to bank clients.

The Board also is adopting two changes to the regulatory language authorizing management consulting activities that were suggested by the public comments. The Board believes that these changes would simplify the regulation's application and that their inclusion in the regulation would be appropriate at this time.

The first suggestion would effect a change in the requirement that bank holding companies disclose to all potential clients the names of all existing client institutions to which they provide management consulting advice located in the same market area(s) as the prospective client institution. It was suggested that the administration of this provision would be simplified by changing "market area(s)" to "county(ies) or SMSA(s)." This change would reduce the compliance and administrative costs of the provision by minimizing uncertainty over the appropriate market definition without significantly reducing the amount of disclosure to prospective clients. The Board believes that the proposed change would improve the regulation and has included it in the final regulation.

The second proposed change that the Board is adopting would automatically permit bank holding companies that have been granted prior approval to offer management consulting services to commercial banks to also offer such services to nonbank depository organizations without the necessity of filing an application. This change was recommended in order to avoid unnecessary applications since the

public benefits considerations upon which the Board based its initial approvals of management consulting services are essentially the same as would apply with respect to applications to offer such services to nonbank institutions. Since the activity in question would be the same and the types of customers would not significantly differ, the Board regards its prior approvals of management consulting activities as extending to the provision of such services to nonbank clients in view of the addition of such clients to Regulation Y.

The Board also is making a technical change in § 225.4(a)(12) of Regulation Y by deleting the requirement in footnote 10 requiring that applications to engage *de novo* in management consulting activities be filed in accordance with the procedures in section 225.4(b)(2) for acquisitions of a going concern. Such applications should be filed in accordance with the procedures in § 225.4(b)(1) for *de novo* activities. This change reflects the Board's actual practice with regard to such applications.

In connection with this action, the Board also is amending Regulation Y to permit bank holding companies to have common management officials with depository institutions to which they provide management consulting services if such interlocks would be permissible under exceptions contained in the Board's Regulation L (Management Official Interlocks) that apply to depository institutions in need of management or operating expertise. 12 CFR 212.4(b). Regulation Y currently provides that bank holding companies may not have officers, directors, or employees in common with banks to which they provide management consulting services. 12 CFR 225.4(a)(12)(ii). The purpose of this restriction is to guard against potential conflicts of interest. An exception is provided when such interlocking relationships are or would be permitted under the exception contained in Regulation L for banks located in low income areas. This exception reflects a determination that the benefits of providing management consulting services to institutions in need of management expertise outweigh any potential conflicts of interest.

The low income exception was incorporated into Regulation Y at the same time that it was added to Regulation L. Since adoption of this exception, other exceptions have been