



FEDERAL RESERVE BANK
OF DALLAS

ROBERT D. McTEER, JR.
PRESIDENT
AND CHIEF EXECUTIVE OFFICER

DALLAS, TEXAS
75265-5906

July 12, 1996

Notice 96-65

TO: The Chief Executive Officer of each member bank and others concerned in the Eleventh Federal Reserve District

SUBJECT

Request for Public Comment on the Proposed Rescission of Regulation R (Relations with Dealers in Securities) and a Related Interpretation

DETAILS

The Board of Governors of the Federal Reserve System is requesting public comment on the proposed rescission of Regulation R (Relations with Dealers in Securities), which the Board believes is no longer necessary. In addition, the Board is proposing to amend its regulations to remove an interpretation of Section 32 of the Glass-Steagall Act, which the Board also believes is unnecessary.

The Board must receive comments by August 2, 1996. Please address comments to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. All comments should refer to Docket No. R-0931.

ATTACHMENT

A copy of the Board's notice as it appears on pages 34749-51, Vol. 61, No. 129, of the *Federal Register* dated July 3, 1996, is attached.

MORE INFORMATION

For more information, please contact Julie Mills at (214) 922-6229. For additional copies of this Bank's notice, please contact the Public Affairs Department at (214) 922-5254.

Sincerely yours,

Robert D. McTeer, Jr.

For additional copies, bankers and others are encouraged to use one of the following toll-free numbers in contacting the Federal Reserve Bank of Dallas: Dallas Office (800) 333-4460; El Paso Branch *Intrastate* (800) 592-1631, *Interstate* (800) 351-1012; Houston Branch *Intrastate* (800) 392-4162, *Interstate* (800) 221-0363; San Antonio Branch *Intrastate* (800) 292-5810.

inspected in room MP-500 between 9 a.m. and 5 p.m., except as provided in § 261.8 of the Board's Rules Regarding Availability of Information, 12 CFR 261.8.

FOR FURTHER INFORMATION CONTACT:

Richard M. Ashton, Associate General Counsel (202/452-3750), or Thomas M. Corsi, Senior Attorney (202/452-3275), Legal Division. For the hearing impaired *only*, Telecommunications Device for the Deaf (TDD), Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:

Section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994 (CDRI Act)

Section 303(a) of the CDRI Act (12 U.S.C. 4803(a)) requires the Board, as well as the other federal banking agencies, to review its regulations and written policies in order to streamline and modify these regulations and policies to improve efficiency, reduce unnecessary costs, and eliminate unwarranted constraints on credit availability. The Board has reviewed its interpretations of section 32 of the Glass-Steagall Act (12 U.S.C. 78) with this purpose in mind, and, as is explained in greater detail in the text that follows, proposes to amend these interpretations in a way designed to meet the goals of section 303(a).

Substantive Provisions of Regulation R

The Board's Regulation R (12 CFR Part 218) implements section 32 of the Glass-Steagall Act. Section 32 prohibits officer, director and employee interlocks between member banks and firms "primarily engaged" in underwriting and dealing in securities, and authorizes the Board to exempt from this prohibition, under limited circumstances, certain interlocks by regulation. Currently, Regulation R restates the statutory language of section 32, and sets forth the only exemption adopted by the Board since passage of the Glass-Steagall Act. The Board also has codified in the CFR 14 interpretations of the substantive provisions of section 32 and the regulation.¹ The Board also has issued other interpretations of section 32 that are contained in the Federal Reserve Regulatory Service (FRRS).

The exemption in Regulation R, adopted by the Board in 1969, permits interlocks between member banks and securities firms whose securities underwriting and dealing activities are limited to underwriting and dealing in only securities that a national bank

would be authorized to underwrite and deal in. The adoption of the express exemption was apparently based on the assumption that the literal language of the section 32 prohibition could at least arguably cover bank-eligible securities activities.

Subsequently, in orders approving applications under the Bank Holding Company Act (12 U.S.C. 1841 et seq.), the Board interpreted the prohibitions of section 20 of the Glass-Steagall Act, which prohibits a member bank from being affiliated with a firm engaged principally in underwriting and dealing in securities, as not applying on their face to underwriting and dealing in securities that may be underwritten and dealt in directly by a state member bank. In these decisions, the Board also expressed the view that section 32 similarly did not cover an interlock between a member bank and a firm that was not engaged in securities activities covered by section 20.² Accordingly, in light of the Board's more recent view of the scope of section 32, the express exemption from the provisions of section 32 for bank-eligible securities activities is no longer necessary.³ Moreover, the Board has never adopted any other exemption to the interlocks provision and historically, requests that the Board create new exemptions have been infrequent and have been uniformly denied.⁴

Since the exemption in Regulation R is no longer necessary, and it is not necessary to have a substantive regulation solely to restate a statutory provision, the Board is proposing to rescind Regulation R.

Bank Holding Company Interpretation of Section 32 of the Glass-Steagall Act

With one exception, the 14 interpretations of section 32 now contained in the CFR, would be retained and transferred to 12 CFR Part 250,

²This interpretation has been upheld by the courts. *Securities Industry Association v. Board of Governors of the Federal Reserve System*, 839 F.2d 47, 62 (2d Cir. 1988), cert. denied, 486 U.S. 1059 (1988).

³The Board is proposing to adopt a new interpretation of section 32 to clarify this point.

⁴A footnote to Regulation R that dates to 1936 makes it clear that a broker who is engaged solely in executing orders for the purchase and sale of securities on behalf of others in the open market is not engaged in the business referred to in section 32. The Board has since authorized bank holding companies to engage in this activity directly, reiterating that securities brokerage is not a proscribed activity under either sections 32 or 20 of the Glass-Steagall Act. *BankAmerica Corporation*, 69 Federal Reserve Bulletin 105 (1983). The courts upheld the Board's interpretation. *Securities Industry Assn. v. Board of Governors*, 468 U.S. 207 (1984). The removal of Regulation R does not affect this interpretation.

FEDERAL RESERVE SYSTEM

12 CFR Parts 218 and 250

[Regulation R; Docket No. R-0931]

Relations With Dealers in Securities Under Section 32, Banking Act of 1933; Miscellaneous Interpretations

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Notice of proposed rulemaking.

SUMMARY: The Board is proposing to amend its regulations to remove Regulation R concerning relations with dealers in securities under section 32 of the Banking Act of 1933, which the Board believes is no longer necessary. The Board also is proposing to amend its regulations to remove an interpretation of section 32 of the Glass-Steagall Act, which the Board believes is no longer necessary. This interpretation explains the position of the Board regarding the application of the prohibitions of section 32 to bank holding companies.

DATES: Comments must be received by August 2, 1996.

ADDRESSES: Comments should refer to Docket No. R-0931 and may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Docket No. R-0931, 20th Street and Constitution Avenue, NW., Washington, DC 20551. Comments addressed to Mr. Wiles may also be delivered to the Board's mail room between 8:45 a.m. and 5:15 p.m., and to the security control room outside of those hours. Both the mail room and control room are accessible from the courtyard entrance on 20th Street between Constitution Avenue and C Street, NW. Comments may be

¹ 12 CFR 218.101-218.114.

which contains miscellaneous Board interpretations.

By their terms, the prohibitions of section 32 apply only to member banks. In 1969, the Board issued an interpretation that extended the prohibitions of section 32 to a bank holding company where the principal activity of the bank holding company is the ownership and control of member banks.⁵ The Board is now seeking public comment on rescinding this interpretation.

The Board based its 1969 interpretation not so much on the literal language of section 32, but on its belief that where the ownership and control of member banks is the principal activity of a bank holding company, the same possibilities of abuse that section 32 was designed to prevent would be present in the case of a director of the holding company as in the case of the member bank.⁶ The Board believed that giving cognizance to the separate corporate entities in such a situation would partially frustrate Congressional purpose in enacting section 32.

The Board now believes that it could rescind this interpretation and give some measure of regulatory burden relief to bank holding companies in a manner consistent with section 32, and without frustrating the Congressional purpose underlying the section. The Board is not barred by the literal terms of the Glass-Steagall Act from rescinding the interpretation. As noted above, section 32 specifically restricts only those interlocks involving member banks. While the bank holding company structure was not in widespread use when section 32 was adopted, Congress has amended section 32 since the section was adopted and since bank holding companies have become commonplace, but never has extended the prohibitions in the section to bank holding companies. Notably, in 1987, Congress extended the prohibitions of section 32 to cover interlocks involving nonmember banks and thrift institutions but not interlocks involving bank holding companies.⁷

The potential that removal of the interpretation could frustrate Congressional purpose in enacting section 32 is mitigated by the fact that the prohibitions of section 32 would

continue to apply to member banks. Accordingly, the directors, officers and employees of these banks, none of whom may be interlocked with a securities firm, could serve as a check against the possibilities of abuse that section 32 is intended to prohibit. In addition, the Board believes that by rescinding this interpretation, it would be granting some measure of regulatory relief to bank holding companies by giving them access to a larger pool of persons from which to choose their officers, directors, and employees.⁸

Other Interpretations of Section 32

The Board also seeks comment on whether any of the other interpretations of section 32 previously adopted by the Board could be amended.

Regulatory Flexibility Act Analysis

Pursuant to section 605(b) of the Regulatory Flexibility Act (Pub. L. 95-354, 5 U.S.C. 601 *et seq.*), the Board of Governors of the Federal Reserve System certifies that adoption of this proposed rule will not have a significant economic impact on a substantial number of small entities that would be subject to the regulation.

This amendment will remove a regulation and an interpretation that the Board believes are no longer necessary. The amendment does not impose more burdensome requirements on bank holding companies than are currently applicable.

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR 1320 Appendix A.1), the Board reviewed the proposed rule under the authority delegated to the Board by the Office of Management and Budget. No collections of information pursuant to the Paperwork Reduction Act are contained in the proposed rule.

List of Subjects

12 CFR Part 218

Antitrust, Federal Reserve System, Securities.

12 CFR Part 250

Federal Reserve System.

For the reasons set forth in the preamble and under the authority of 12 U.S.C. 248, the Board proposes to amend Chapter II of the Code of Federal Regulations as set forth below:

⁸ Should the Board determine to rescind this interpretation, this action would not affect other Board decisions or determinations that restrict interlocks to ensure compliance with section 20 of the Glass-Steagall Act (12 U.S.C. 377). See, e.g., *Mellon Bank Corporation*, 79 Federal Reserve Bulletin 626 (1993).

PART 218—[AMENDED]

§§ 218.101 through 218.113 [Redesignated as §§ 250.400 through 250.412]

1. Sections 218.101 through 218.113 are redesignated as set forth in the following table:

Old Section	New section
218.101	250.400
218.102	250.401
218.103	250.402
218.104	250.403
218.105	250.404
218.106	250.405
218.107	250.406
218.108	250.407
218.109	250.408
218.110	250.409
218.111	250.410
218.112	250.411
218.113	250.412

PART 218—[REMOVED]

2. Part 218 is removed.

PART 250—MISCELLANEOUS INTERPRETATIONS

1. The authority citation for part 250 is revised to read as follows:

Authority: 12 U.S.C. 78, 248(i) and 371c(e).

2. A new center heading is added immediately preceding newly designated § 250.400 to read as follows:

Interpretations of Section 32 of the Glass-Steagall Act

3. Section 250.413 is added to read as follows:

§ 250.413 "Bank-eligible" securities activities.

Section 32 of the Glass-Steagall Act (12 U.S.C. 78) prohibits any officer, director, or employee of any corporation or unincorporated association, any partner or employee of any partnership, and any individual, primarily engaged in the issue, flotation, underwriting, public sale, or distribution, at wholesale or retail, or through syndicate participation, of stocks, bonds, or other similar securities, from serving at the same time as an officer, director, or employee of any member bank of the Federal Reserve System. The Board is of the opinion that to the extent that a company, other entity or person is engaged in securities activities that are expressly authorized for a state member bank under section 16 of the Glass-Steagall Act (12 U.S.C. 24(7), 335), the company, other entity or individual is not engaged in the types of activities described in section 32. In addition, a securities broker who is engaged solely in executing orders for the purchase and

⁵ 12 CFR 218.114.

⁶ As noted in the Board's interpretation, section 32 is directed to the probability or likelihood that a bank director interested in the underwriting business may use his or her influence in the bank to involve it or its customers in securities sold by his or her underwriting house.

⁷ The provisions extending the prohibitions of section 32 to nonmember banks and thrifts expired in 1988.

sale of securities on behalf of others in the open market is not engaged in the business referred to in section 32.

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

Date: June 26, 1996.

William W. Wiles,
Secretary of the Board.

[FR Doc. 96-16841 Filed 7-02-96; 8:45am]

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