FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 6805]
[September 21, 1971]

BANK HOLDING COMPANIES

Amendments to Regulation Y, Effective September 21, 1971

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

The following statements were made public yesterday by the Board of Governors of the Federal Reserve System:

Control of a Bank or Other Company

The Board of Governors of the Federal Reserve System today announced the rules it will follow in determining when a company exercises control over a bank or other company, in the light of the 1970 amendments to the Bank Holding Company Act.

Under the original Bank Holding Company Act of 1956, only those holding companies that controlled 25 per cent or more of the voting shares of a bank holding company or of two or more banks, or controlled the election of a majority of the directors of each of two or more banks, were required to register with the Federal Reserve and limit their activities to banking and closely related activities.

The 1970 amendments, in part, extended the provisions of the Act to holding companies controlling only one bank and gave the Board greater latitude to determine when control exists.

To carry out the control provisions of the Act, the Board has established as part of its Regulation Y a series of presumptions regarding control of a bank or other company, based on its 15 years' experience in administering the Act. These presumptions, with certain exceptions, are generally those that were proposed by the Board on July 1. The proposals not included in the regulation will serve as guidelines to the Reserve Banks for investigation of control in individual cases. The regulation also reflects the control provisions of the original Act and the 1966 amendments.

Under the Act and regulation, it is a conclusive presumption that a company controls a bank or other company, if:

1. It directly or indirectly owns, controls or has the power to vote 25 per cent or more of any class of voting securities of the bank or other company.

2. It controls in any manner the election of a majority of the directors or trustees of the bank or company.

The Act and regulation also state that shares owned or controlled by any subsidiary of a bank holding company are indirectly owned or controlled by the holding company itself, and that shares held by trustees for the benefit of a company, its shareholders or its employees, are controlled by that company.

In addition the Board has determined that common control exists whenever 25 per cent or more of any class of voting securities of a company are stapled or otherwise joined with 25 per cent or more of any class of voting securities of another company whether pursuant to an agreement, by-law, article of incorporation or other means.

The Board also listed a series of rebuttable presumptions and outlined the procedures to be used for determining control in such cases or in any other case where it appears to the Board that control exists. The Board emphasized, however, that the existence of control in any given instance, whether found on the basis of one or more presumptions or otherwise, would not prejudice the Board's action on any application for approval of the acquisition of shares by the company having control. In other words, a company having control of a bank has no automatic right to acquire shares in the controlled bank without the approval of the Board. In any application for such approval, the existence of such control would merely be one of the factors which the Board would take into consideration, not necessarily favorably, in reaching its decision.

The Act itself establishes a rebuttable presumption of control where ownership of shares was transferred after January 1, 1966, by a bank holding company — or by a company that would be a bank holding company except for the transfer — in circumstances in which the recipient of the shares can be regarded as under the control of the company making the transfer.

In addition, the Board's regulation will establish the following rebuttable presumptions of control of a bank or other company:

1. Where a company controls more than 5 per cent of any class of voting securities of a bank or other company if either of the following conditions exists:

(a) The company has an interlock with the bank or other company through one or more directors, trustees, partners, or officers or employees with policymaking functions, and no other person controls as much as 5 per cent of any class of voting securities of the bank or other company.

(b) Additional voting securities are controlled by individuals (or members of their immediate families) who are directors, officers, trustees or partners of the company, and the individual securities plus those held by the company total 25 per cent or more of any class of voting securities of the bank or second company. Directors, officers, trustees or partners who own 25 per cent or more of any class of voting securities of the bank or other company would also be covered by this presumption.

(The above presumption does not apply when voting securities of a bank or other company are held in a fiduciary capacity and the company does not have sole discretionary authority to exercise the voting rights.)

2. Where a company, or any of its subsidiaries, which, by virtue of an agreement or understanding, exercises a significant influence over the management or over-all operations of a bank or other company.

3. Where a company enters into an agreement — which involves shares constituting control — restricting in any manner the rights of a holder of voting securities of a bank or other company, except that the presumption does not apply to agreements among shareholders granting each other a right of first refusal with respect to their shares, agreements incident to a bona fide loan transaction or agreements restricting transfers temporarily while awaiting approval of an acquisition by a Federal bank supervisory agency.

4. Where a company owns securities that are immediately convertible at the option of the holder or owner into voting securities and the amount of the voting securities involved would constitute control of the bank or other company under the criteria of the regulation.

Under procedures spelled out in the regulation, the Board will inform a company by letter that a preliminary determination of control has been made. The company has 30 days — or longer if permitted by the Board — to (a) indicate its willingness to end the control relationship and furnish a specific plan to do so, (b) state that it will seek Board approval to retain the shares, register, report the controlled company as a subsidiary or otherwise comply with the Act, or (c) set forth any facts and circumstances to support its contention that control does not exist.

A company may request a hearing to contest the Board's preliminary determination of control.

Several rebuttable presumptions that were proposed by the Board will serve as guidelines to the Reserve Banks for ascertaining possible areas of control, although they are not formally a part of the regulation.

The Reserve Banks will conduct investigations to determine the question of control in the following situations:

1. Whenever a partnership has significant interests in a bank or bank holding company.

2. Where a company controls at least 10 per cent of the shares of each of two banks or 5 per cent of the shares of each of three or more banks.

3. Where a bank makes loans secured by bank stock at terms more favorable to the borrower than should otherwise be expected.

Foreign Activities of Domestic Holding Companies

The Board of Governors of the Federal Reserve System today announced the types of foreign business activities in which domestic bank holding companies may engage under the 1970 amendments to the Bank Holding Company Act.

An amendment to the Board's Regulation Y will permit bank holding companies to acquire ownership or control of the shares of companies in which Edge Act corporations may invest. Such acquisitions must be made with the Board's consent under procedures similar to those presently governing investments by Edge Act corporations.

Edge Act corporations are generally subsidiaries of member banks, established in the United States with specific Board approval, to facilitate the foreign business of their parent banks. The corporations are permitted to exercise broader powers in foreign operations than are their parent banks. In general, Edge Act corporations may invest in companies engaged in international or foreign banking or other international or foreign financial operations. They may also have minority non-controlling investments in other types of companies, when the size of the investment is proportionate to a proper financing activity. The Edge Act was enacted by Congress in 1919.

The regulatory amendment, which is effective tomorrow, is similar to a proposal made by the Board on June 16. It implements the Board's authority under section 4(c)(13) of the Bank Holding Company Act to permit bank holding companies to acquire shares of companies which do no business in the

United States except as an incident to such companies' international or foreign business. The Board has acted on the basis of its determination that it would be consistent with the purposes of the Act and in the public interest to permit bank holding companies to engage in the kinds of activities permissible to Edge Act corporations.

The regulatory amendment would not authorize bank holding companies to acquire shares of companies that accept deposits in the United States.

In submitting the amendment on foreign business activities for publication in the *Federal Register,* the Board of Governors issued the following additional statement:

By notice of proposed rule making published in the Federal Register on June 23, 1971 (36 F. R. 11944), the Board of Governors proposed to implement its regulatory authority under section 4(c)(13) of the Bank Holding Company Act to permit bank holding companies, under certain conditions, to invest in companies that do no business in the United States except as an incident to their international or foreign business and the shares of which are eligible for investment by Edge Act corporations.

Following consideration of the comments received, the Board has determined that it would be consistent with the purposes of the Act and in the public interest to permit bank holding companies to acquire ownership or control of the shares of companies in which Edge Act corporations may invest, if such acquisitions are made with the Board's consent under procedures similar to those presently governing investments by Edge Act corporations.

Under this approach, the standards of section 25(a) of the Federal Reserve Act would govern the kinds of activities in which holding companies may engage on the basis of section 4(c)(13) of the Bank Holding Company Act. The Board has interpreted section 25(a) to authorize companies organized thereunder to engage in international or foreign banking, other international or foreign financing activities, and activities that are incidental thereto or, in the Board's judgment, are usual in the business of banking in the foreign countries where the activities are conducted. Such companies may not, however, engage in the business of underwriting, selling or distributing securities in the United States or trade in commodities. In practice, companies organized under section 25(a) have generally been permitted to have minority noncontrolling investments in any companies that do no business in the United States except as an incident to their international or foreign business when the size of the investment is proportionate to a proper financing activity, but otherwise to invest only in companies that limit their activities to the kinds of activities in which companies organized under section 25(a) may themselves engage.

Under this approach, limitations applicable to Edge Act corporations governing the extent to which and the manner in which they may conduct their permissible activities are generally inapplicable to activities conducted on the basis of section 4(c)(13). Such limitations include minimum capitalization requirements, capital and surplus limitations on investments, approval requirements respecting issuance abroad of debentures, bonds or notes, and limitations and restrictions respecting acceptance liabilities, liabilities of one borrower, and aggregate liabilities.

The Board nevertheless retains authority to impose conditions regarding the operations of foreign subsidiaries of domestic bank holding companies similar to those conditions that it deems prudent to impose upon Edge Act corporations and their foreign subsidiaries. Bank holding company subsidiaries engaged in foreign activities would, in any case, specifically be required to obtain the Board's approval for the establishment of branches or agencies in the United States or of banking branch offices in any foreign country new to their operations and for the issuance in the United States of any debentures, bonds, promissory notes, or similar obligations, other than instruments or obligations due within one year.

As a matter of policy, the Board considers that, in general, bank holding companies seeking to engage in foreign banking activities that involve the receipt of deposits in the United States should do so through Edge Act corporations or Agreement corporations.

Enclosed is a copy of the amendments to Regulation Y referred to in the above statements. Additional copies will be furnished upon request.

Alfred Hayes,
President.

Board of Governors of the Federal Reserve System

BANK HOLDING COMPANIES

AMENDMENTS TO REGULATION Y

1. Effective September 21, 1971, paragraphs (c) and (d) of section 222.3 are deleted, and section 222.2 is amended to read as follows:

SECTION 222.2 — DETERMINATIONS REGARDING CONTROL

(*a*) **Conclusive presumptions of control.** — Conclusive presumptions that a company controls a bank or other company are established by section 2(a)(2)(A) and (B) and by section 2(g)(1) and (2) of the Act. In addition, the Board has determined that, whenever the transferability of 25 per cent or more of any class of voting securities of a company is conditioned in any manner, whether pursuant to an agreement, by-law, article of incorporation, or otherwise, upon the transfer of 25 per cent or more of any class of voting securities of another company, the holders of the securities affected by the condition (that is, those who hold both the securities whose transferability is so conditioned and the securities whose transfer can be required to satisfy the condition) constitute, in their capacity as such, a "company" for the purposes of the Act unless one of the issuers of such securities is a subsidiary of the other and is so identified in an order of the Board or in a registration statement or report accepted by the Board under the Act.

(*b*) **Rebuttable presumptions of control.** — A rebuttable presumption that a company controls a bank or other company is established by section 2(g)(3) of the Act. In addition, the Board has established, for use in proceedings instituted in accordance with the procedures of paragraph (c) below, the following rebuttable presumptions:

(1) A company that owns, controls, or has power to vote more than 5 per cent of any class of voting securities of a bank or other company (except where such securities are held in a fiduciary capacity

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and the company does not have sole discretionary authority to exercise the voting rights) presumably controls that bank or other company if (i) one or more of the company's directors, trustees, or partners, or officers or employees with policymaking functions serves in any of these capacities with the bank or other company, and (ii) no other person owns, controls, or has power to vote as much as 5 per cent of any class of voting securities of that bank or other company.

(2) A company that owns, controls, or has power to vote more than 5 per cent of any class of voting securities of a bank or other company (except where such securities are held in a fiduciary capacity and the company does not have sole discretionary authority to exercise the voting rights) presumably controls that bank or other company if additional voting securities are owned, controlled, or held with power to vote by individuals (or members of their immediate families as defined in § 206.2(k) of this chapter (Regulation F)) who are directors, officers, trustees, or partners of the company (or own, directly or indirectly, 25 per cent or more of any class of voting securities of the company) and, together with the company's securities, aggregate 25 per cent or more of any class of voting securities of that bank or other company.

(3) A company that enters into any agreement or understanding with a bank or other company (other than an investment advisory agreement), such as a management contract, pursuant to which the company or any of its subsidiaries exercises significant influence with respect to the general management or overall operations of the bank or other company presumably controls such bank or other company.

(4) A company that enters into any agreement or understanding under which the rights of a holder of voting securities of a bank or other company are restricted in any manner presumably controls the shares involved, unless the agreement or understanding (i) is a mutual agreement among shareholders granting to each other a right of first refusal with respect to their shares, or (ii) is incident to a *bona fide* loan transaction, or (iii) relates to restrictions on transferability and continues only for such time as may reasonably be necessary to obtain approval from a Federal bank supervisory authority with respect to acquisition by the company of such securities.

(5) A company that owns directly or indirectly securities that are immediately convertible at the option of the holder or owner thereof into voting securities presumably owns or controls the voting securities.

(*c*) **Procedures for determining control.** — (1) In any case in which a presumption established by paragraph (b) applies, or in any other case where it appears to the Board that a company exercises a controlling influence over the management or policies of a bank or other company, and the company has not complied with the provisions of the Act, the Board may inform the company that a preliminary determination of control has been made on the basis of the facts summarized in the communication. Such company shall within 30 days (or such longer period of time as may be permitted by the Board) (i) indicate to the Board its willingness to terminate the control relationship and to furnish promptly its specific plan to do so; or (ii) state that it will promptly seek Board approval to retain the control relationship, or, if the control relationship has existed continuously since prior to December 31, 1970 (in a manner not covered by § 2(a)(2)(A) or (B)), that it will register as a bank holding company or, if already a holding company, report the bank or other company as a subsidiary, or otherwise comply with the applicable provisions of the Act; or (iii) set forth such facts and circumstances as may support its contention that there is not a control relationship.

(2) A company may request a hearing to contest the Board's preliminary determination of control. In the event a hearing is held, any applicable presumptions established by paragraph (b) shall be considered in the usual manner in accordance with the rules of evidence, and the Board will by order, on the basis of the record of the hearing, decide the issues involved and direct such action as may be necessary or appropriate in the circumstances. In the event no hearing is held, but the preliminary determination of control is contested, the Board will decide the matter on the basis of the evidence available to it, relying on the presumptions established in paragraph (b), and will by order direct such action as may be necessary or appropriate in the circumstances.

2. Also effective September 21, 1971, section 222.4 is amended by adding a new paragraph (f) to read as follows:

SECTION 222.4 — NONBANKING ACTIVITIES

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(*f*) **Foreign activities of domestic holding companies.**

(1) Any bank holding company may, with the consent of the Board, own or control voting shares of any company in which a

company organized under section 25(a) of the Federal Reserve Act (12 U.S.C. 611-631) may invest other than a company that accepts deposits or similar credit balances in the United States.

(2) The procedures governing the Board's consent shall be the same as those set forth in § 211.8 of this chapter (Regulation K). In addition, the Board grants its general consent for any bank holding company to acquire from any of its subsidiaries any shares the subsidiary holds with the consent of the Board pursuant to parts 211 or 213 of this chapter (Regulations K and M). The Board may at any time, upon notice, suspend the general consent procedures with respect to any bank holding company or with respect to the acquisition of shares of companies engaged in particular kinds of activities.

(3) It shall be a condition to the Board's specific consent to the continued holding of voting shares of any subsidiary of a bank holding company which are acquired or held on the basis of an exemption under section 4(c)(13) of the Act that the subsidiary may take the following actions only with prior Board approval: (a) establish branch offices or agencies in the United States or to engage in receiving deposits in any foreign country (other than a foreign country in which it already has such an activity with the Board's approval) or (b) issue in the United States any debentures, bonds, promissory notes, or similar obligations, other than instruments or obligations due within one year.

(4) A bank holding company shall inform the Board, through its Federal Reserve Bank within 30 days after the close of each semi-annual period, of all shares acquired or disposed of during that period that are or were held under the authority of this subsection. With respect to any acquisition, such information shall (unless previously furnished) include brief descriptions of the business of the companies whose shares were acquired.