FEDERAL RESERVE BANK OF NEW YORK

[Circular No. **9355**
September 2, 1982]

REGULATION Y

Amendment and Interpretation on Permissible Data Processing Activities of Bank Holding Companies

To All Bank Holding Companies, and Others Concerned,
in the Second Federal Reserve District:

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board has amended its Regulation Y (bank holding companies) and related interpretation to clarify and expand the data processing activities permissible for bank holding companies.

The Board's action followed approval in July, by order, of an application by Citicorp to engage in similar expanded data processing activities. The Board's order approving the Citicorp application, and its amendment of Regulation Y, reflect the Board's consideration of public comment, a public hearing and the findings of the Administrative Law Judge who conducted the hearings.

The Board's actions are set forth in the attached official notice and are related to previous provisions of Regulation Y, previous Board bank holding company actions, the amendment of Regulation Y as proposed for comment and the law judge's determinations. Highlights are:

— For the internal operations of the bank holding company or the internal operations of its subsidiaries, services provided may include data processing and data transmission, including provision of data processing hardware, software, documentation and operating personnel.

— For others, a bank holding company may provide — when certain specified conditions are met — data processing and transmission services, facilities (defined to include hardware, software, documentation and operating personnel) or data bases, provided by any technologically feasible means, on condition that the data to be processed are financial, banking or economic data.

In an accompanying interpretation, the Board specified that in providing packaged data processing and transmission facilities a bank holding company should provide facilities only for the performance of banking functions, such as check collection and the like, for depository or similar institutions, such as mortgage companies. The Board interpreted its regulation expanding permissible data processing services to include as incidental activities the provision of excess data processing capacity under specified restrictions, and the provision of by-products of permissible data processing and transmission activities where they are not designed or appreciably enhanced for marketing purposes.

The Board's action is effective September 25, 1982.

Enclosed is an excerpt from the *Federal Register* of August 26, 1982, containing the text of the amendment and interpretation. Questions thereon may be directed to our Domestic Banking Applications Department (Tel. No. 212-791-5861).

ANTHONY M. SOLOMON,
President.

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Board of Governors of the Federal Reserve System

BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL

AMENDMENT AND INTERPRETATION OF REGULATION Y

(Effective September 25, 1982)

FEDERAL RESERVE SYSTEM

12 CFR Part 225

[Docket No. R-0363]

Bank Holding Companies and Change in Bank Control, Data Processing, and Electronic Funds Transfer Activities

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule and interpretation.

SUMMARY: The Board of Governors of the Federal Reserve System is amending its Regulation Y which concerns bank holding companies and changes in bank control, and related interpretation to clarify and expand the scope of permissible data processing activities in which a bank holding company may engage. The revised interpretation describes certain activities the Board considers incidental to permissible data processing and data transmission activities. The new activities include the transmission of data, the provision of data bases, and the provision of data processing hardware in conjunction with permissible software.

EFFECTIVE DATE: September 25, 1982.

FOR FURTHER INFORMATION CONTACT: Richard M. Ashton, Assistant General Counsel (202) 452-3750, or Jennifer Johnson, Senior Attorney (202) 452-3584, 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."[1] Section 225.4(a)(8) of the Board's Regulation Y currently provides that certain data processing activities are closely related to banking and thus permissible for bank holding companies under section 4(c)(8). In 1971, the Board issued an interpretation, which was amended in 1975 (12 CFR 225.123(e)) and stated, among other things, that bank holding companies may perform certain incidental activities necessary to carry on permissible data processing activities.

I. Background

In 1979, Citicorp, New York, New York, applied to the Board for approval to engage in expanded data processing and data transmission activities, and requested the Board to amend Regulation Y in a manner that would specifically permit Citicorp's proposed activities. The application and proposed amendment to Regulation Y were protested by the Association of Data Processing Service Organizations, Arlington, Virginia ("ADAPSO"), and other interested organizations[2] (collectively "Protestants"). On July 22, 1981, the Board published the proposed amendment for public comment and specifically requested comments from those interested persons who did not wish to participate in the formal hearing.

In accordance with the Board's Rules of Practice for Hearings (12 CFR Part 263), a public administrative hearing on the application and proposed rule was held before an Administrative Law Judge. The Administrative Law Judge also considered all the comments received concerning the proposed amendment from interested persons who did not participate in the hearing.

On March 29, 1982, the Administrative Law Judge, after an evaluation of all of the facts of record in this matter, determined that each of the eight activities proposed by Citicorp is closely related to banking and thus permissible for bank holding companies, and recommended that the Board adopt the proposed amendment to Regulation Y, with certain limitations.

On July 9, 1982, the Board, acting by order, approved Citicorp's application to engage in eight categories of data processing and data transmission activities, finding that each activity, as discussed and limited in the order, is

[1] In *National Courier Association* v. *Board of Governors of the Federal Reserve System*, 516 F.2d 1229 (D.C. Cir. 1975), the court established guidelines to determine whether a particular activity meets the "closely related to banking" test. Under these guidelines an activity may be found to be closely related to banking if it is demonstrated that banks generally (1) have in fact provided the proposed service; or (2) provide services that are operationally or functionally so similar to the proposed services as to equip them particularly well to provide the proposed service; or (3) provide services that are so integrally related to the proposed service as to require their provision in a specialized form.

[2] Other Protestants to the application were Electronic Data Systems Corporation; ADP Network Services, Inc.; Comshare, Inc.; National CSS, Inc.; Quantum Computer Services, Inc.; Tymshare, Inc.; and On-Line Systems, Inc., which subsequently withdrew from the proceeding.

For this Regulation to be complete, retain:

1) Regulation Y pamphlet, as amended effective April 5, 1978.
2) Rescission of part of Regulation Y, effective June 14, 1979.
3) Amendments effective January 1, 1979, March 10, 1979, October 24, 1979, December 5, 1979, December 31, 1980, January 3, 1981, January 7, 1981, September 1, 1981, December 21, 1981, April 5, 1982, and April 20, 1982.
4) This slip sheet.

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either closely related to banking or a permissible incidental activity.[3]

II. Description of the Amendment and Revised Interpretation

Consistent with its approval of the Citishare application, the Board is adopting the amendment to Regulation Y proposed with the application, with the modifications recommended by the Administrative Law Judge and with other modifications explained below. The amendment will make it permissible for bank holding companies to engage in the data processing and transmission services the Board has approved by order in the *Citishare* case.[4] The Board's findings on the permissibility of the services involved are set forth in detail in the Board's *Citishare* order.

A. Permissible Services for Internal Operations

Currently, under Regulation Y, a bank holding company may provide bookkeeping or data processing services for the internal operations of the holding company or its subsidiaries. The proposed amendment would expand the types of services provided for internal operations to include data transmission, information, and facilities.[5] The Administrative Law Judge recommended adoption of this revision.

With one modification, the Board adopts this recommended amendment. It has not been contested that data processing services for the internal use of a bank holding company are closely related to banking. Indeed, such activities are permissible as servicing activities pursuant to section 4(c)(1)(C) of the Act. The Board is concerned, however, that the term "information" as used in the recommended amendment is vague and does not describe the permissible activities with sufficient specificity. It is apparent from Citicorp's application that the use of the term "information" in the proposed amendment was intended to permit providing access to data bases compiled by the holding company. In order to reduce potential ambiguity concerning permissible activities, the final amendment substitutes the term "data bases" for "information."

B. Permissible Services for Others

Services that may be provided to others under the current regulation are limited to storing and processing permissible data, *i.e.*, banking, financial, and related economic data. The proposed amendment, as modified by the Administrative Law Judge, would permit processing and transmitting permissible data, and providing information and facilities for such data. The proposed amendment would also permit access to such services, information, or facilities by any technologically feasible means. The Administrative Law Judge concluded that data processing and transmission services, as well as providing information and facilities, are closely related to banking within certain limitations that he recommended be adopted.

Protestants object to this finding, arguing that the Administrative Law Judge erred by not applying the *National Courier* tests to the technologies bank holding companies would use to process and transmit permissible data. As explained in the *Citishare* decision, however, the Board has consistently taken the position in previous actions regarding data processing activities that the particular technology by which a data processing activity is provided is not determinative of whether the activity is permissible. In its *Decimus* decision, the Board expressly stated that permissible data processing activities may be provided by any technologically feasible method.[6] In the Board's view, the technology is not an activity in itself but a means of providing services that the record indicates are closely related to banking.

Regulation Y, as amended, therefore, incorporates the Recommended Decision's description of permissible types of services, including the recommended provision that such services be provided by any technologically feasible means. However, for the reasons explained above in connection with internal services, the term "data bases" replaces "information" in the revised regulation.

C. Types of Data

The current regulation permits storing and processing of "banking, financial and *related economic data.*" (Emphasis supplied). The proposed amendment would permit data processing activities with regard to "banking, financial and *economic related data.*" The Administrative Law Judge concluded that this portion of the proposed amendment should be adopted.

Protestants object to this finding, asserting that *economic related data* is too broad a category and includes data that are not closely related to banking. The substance of this objection was repeated by other commentors who did not participate in the administrative proceeding. As stated in the *Citishare* decision, the Board agrees that "economic related data" implies a significant expansion of the type of data permitted to be processed by bank holding companies. The Recommended Decision contains no conclusion or finding that supports such a significant expansion of the type of data permitted to be processed. However, the record in this proceeding supports a finding that banks process *economic* data. Accordingly, the amendment as adopted provides that the designated data processing services are permissible where the data to be processed or furnished are banking, financial, or economic.[7]

D. Other Limitations on Permissible Services

As proposed, the amendment to Regulation Y contained no specific limitations on the types of data processing activities permitted. Protestants and the other commentors raised the objection that modern data processing and transmission technologies are such that customers may modify the services and equipment provided to enable the processing of impermissible data. In response to this objection, the Recommended Decision included a limitation in the amendment,

[3] *Citicorp* ("Citishare") 68 *Federal Reserve Bulletin* (July 9, 1982).

[4] These activities are: (1) Data processing through timesharing; (2) on-site data processing; (3) electronic funds transfer and information exchange; (4) home banking; (5) authentication; (6) data processing for the internal operation of Citicorp and its subsidiaries; (7) the sale of by-products of permissible data processing activities, and (8) the sale of excess capacity on data processing and data transmission facilities.

[5] The term data processing "facilities" is defined to include hardware, software, documentation, and operating personnel.

[6] *BankAmerica Corp.* (Decimus Corp.) 66 *Federal Reserve Bulletin* 511, 513 (1980).

[7] Protestants also claim that processing financial and economic data is not closely related to banking because, by definition, such data are not banking data. However, the facts of record indicate that data processing activities of banks today are not limited to banking data but extend to other types of financial and economic data. The Board finds, therefore, under the *National Courier* standards, that processing of "banking, financial and economic data" is closely related to banking.

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which the Board adopts, that all data processing services must be provided pursuant to a written agreement that describes and limits the services to permissible activities. The Board also adopts the Recommended Decision's requirement that all data processing facilities provided by a bank holding company must be designed and marketed for permissilbe data.[8] Moreover, consistent with the Board's finding on this matter in the *Citishare* decision,[9] the amendment also provides that such facilities must also be *operated* for processing and transmitting permissible data. As the Board explained in its order, the data processing industry has the technological capability to limit the use of facilities to permissible data and the Board believes that a bank holding company should take all technical steps necessary to ensure that its facilities are operated only with respect to banking, financial, and economic data.

E. Provision of Hardware

The current regulation does not expressly permit bank holding companies to provide data processing hardware. The proposed amendment would include data processing hardware as part of the facilities permitted to be offered by a bank holding company.

The Administrative Law Judge, finding that it is only questionably economically feasible to offer data processing software without including hardware as part of the service, recommended that Regulation Y be amended expressly to include the provision of hardware under the limitations that such hardware may be offered only in conjunction with software designed and marketed for the processing and transmission of permissible data and that such hardware may not constitute the predominant part of the package. Protestants object to this recommendation asserting that hardware is a separate product from software and that it is not necessary to sell the two products as a package. Other commentors also assert that the provision of data processing hardware is not closely related to banking.

As the Board found in the *Citishare* decision, the record of this proceeding indicates that customers of data processing services require that suppliers provide them with both hardware and software as an integrated package.[10] Where hardware is required to be provided in a specialized form, such as an Automated Teller Machine, its provision meets the third *National Courier* test and is closely related to banking. However, the Board believes that the provision of general purpose hardware is permissible only as an incidental activity. As explained in the *Citishare* decision, the Board believes that a bank holding company may offer general purpose data processing hardware in conjunction with permissible data processing services only if the cost to the bank holding company of such hardware does not exceed approximately 30 per cent of the total cost of the services provided.[11] The amendment adopted by the Board incorporates the limitations on the provision of hardware recommended by the Administative Law Judge, but provides that general purpose hardware provided as a part of a package of data processing services may not constitute more than 30 per cent of any packaged offering.

F. On-site Data Processing Packages

In its *Citishare* decision, the Board found that providing packaged financial systems, including data processing hardware and software, to be installed on the premises of the customer is closely related to banking. Citishare's on-site activities were, however, somewhat limited in scope, since Citishare intended to offer such services to depository or other institutions to perform only banking or banking-related functions, such as check collection or trust department securities recordkeeping. The record on this application and on the proposed amendment was generally restricted to these limited types of on-site data processing services. The Board is concerned that, by its literal terms, the recommended amendment would permit a bank holding company to provide packaged data processing services to *non-depository* institutions to perform *non-banking* related functions. These functions are beyond the scope of the proposal considered by the Board in the Citishare application and the Board has, accordingly, expressed no opinion on the permissibility of such activities. The Board is, therefore, incorporating into its interpretation regarding permissible data processing activities, 12 CFR 225.123(e),[12] a statement that a bank holding company should limit its provision of on-site packaged services to customers that are depository or similar institutions and to providing facilities that perform only banking or banking related functions. This limitation is premised solely on the limited nature of the record before the Board in this proceeding and is not intended to preclude a bank holding company from demonstrating in another case that providing on-site data processing packages to non-depository customers is closely related to banking.

G. Excess Capacity

The sale of excess computer time is currently treated in the Board's data processing interpretation as an incidental activity.[13] The interpretation currently permits a bank holding company to make excess computer time available to anyone so long as the only involvement of the holding company is furnishing the facility and the necessary operating personnel. The proposed amendment would incorporate into Regulation Y a provision permitting the sale of excess capacity on both data processing and data transmission equipment and facilities used in connection with permissible data processing and transmission activities. The Recommended Decision adopted the proposed excess capacity provision but included three limitations on the sale of excess capacity. First, a bank holding company may not purchase data processing equipment solely for the purpose of creating excess capacity. Second, a bank holding company may not sell hardware in connection with excess capacity, and third, a bank

[8] Protestants have raised various other objections to the proposed regulation and the Citishare proposal on the grounds that the activities permitted are not closely related to banking. The Board discussed these objections in detail in its order approving the Citishare proposal and the Board's findings on the objections are specifically incorporated by reference herein.

[9] *Citicorp* ("Citishare") footnote 3, *supra*.

[10] *Citicorp* ("Citishare"), footnote 3, *supra*.

[11] As explained in the *Citishare* decision, the Board expects that in computing relative costs for the purpose of applying this limitation all costs, both direct and indirect, of each component of the package, including the development costs, must be taken into account and the cost of each component will reflect only the cost attributable to that component.

[12] The provisions of the current interpretation concerning the type of data for which processing services may be offered and the development of programs are superseded by provisions in the amended regulation and have been removed.

[13] 12 CFR 225.123(e).

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data bases or access to such services, facilities, or data bases by any technologically feasible means, where:

(A) Data to be processed or furnished are financial, banking or economic, and the services are provided pursuant to a written agreement so describing and limiting the services;

(B) The facilities are designed, marketed, and operated for the processing and transmission of financial, banking or economic data; and

(C) Hardware in connection therewith is offered only in conjunction with software designed and marketed for the processing and transmission of financial, banking or economic data, and where the general purpose hardware does not constitute more than 30 percent of the cost of any packaged offering.

II. Section 225.123(e) is amended by revising the introductory paragraph, paragraph (e)(1) and (e)(2), and by adding a new undesignated paragraph to follow paragraph (e)(4) to read as follows:

§ 225.123 Activities closely related to banking

* * * * *

(e) *Data Processing:* In providing packaged data processing and transmission services for banking, financial and economic data for installation on the premises of the customer, as authorized by § 225.4(a)(8)(ii), a bank holding company should limit its activities to providing facilities that perform banking functions, such as check collection, or other similar functions for customers that are depository or other similar institutions, such as mortgage companies. In addition, the Board regards the following as incidental activities necessary to carry on the permissible activities in this area:

(1) Providing excess capacity, not limited to the processing or transmission of banking, financial or economic data on data processing or transmission equipment or facilities used in connection with permissible data processing and data transmission activities, where:

(A) equipment is not purchased solely for the purpose of creating excess capacity;

(B) hardware is not offered in connection therewith; and

(C) facilities for the use of the excess capacity do not include the provision of any software, other than systems software (including language), network communications support, and the operating personnel and documentation necessary for the maintenance and use of these facilities.

(2) Providing by-products of permissible data processing and data transmission activities, where not designed, or appreciably enhanced, for the purpose of marketability.

(3) * * *

* * * * *

In order to eliminate or reduce to an insignificant degree any possibility of unfair competition where services, facilities, by-products or excess capacity are provided by a bank holding company's nonbank subsidiary or related entity, the entity providing the services, facilities, by-products and/or excess capacity should have separate books and financial statements, and should provide these books and statements to any new or renewal customer requesting financial data. Consolidated or other financial statements of the bank holding company should not be provided unless specifically requested by the customer.

By order of the Board of Governors of the Federal Reserve System, effective August 20, 1982.

William W. Wiles,

Secretary of the Board.

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holding company may provide only limited types of software in connection with its sale of excess capacity.[14]

In recommending that the portion of the amendment relating to excess capacity be adopted, the Administrative Law Judge determined that the sale of excess capacity is closely related to banking. Protestants object to this finding and the Board agrees that Protestants are technically correct. The Board believes that providing excess capacity should continue to be treated as a permissible incidental activity. No evidence was introduced in the record of this proceeding that would support a finding that the sale of excess capacity, which under the recommended amendment may be provided for any type of data, is closely related to banking.

Several commentors on the proposed amendment asserted that it is technologically possible to limit the need for excess capacity unless poor planning is involved. These comments also asserted that excess capacity could be created artificially for the purpose of developing an impermissible data processing/communication system. The record of this proceeding shows that data processors that process time-sensitive data must maintain sufficient capacity to meet peak demand and provide back-up capacity in case of equipment failure. Excess capacity necessarily results from these requirements, and the sale of such excess capacity is necessary to reduce costs and remain competitive.[15] The Board believes that the record of this proceeding concerning excess capacity, as discussed in the *Citishare* decision, demonstrates the necessity of the maintenance and sale of excess capacity and its permissibility as an incidental activity. Furthermore, the Board believes that the limitations recommended by the Administrative Law Judge, which the Board adopts, are sufficient to ensure that the sale of excess capacity is limited to a permissible incidental activity. Since the Board has determined that the sale of excess capacity is an incidental and not a closely related activity, the provisions and limitations recommended by the Administrative Law Judge concerning excess capacity are incorporated into the data processing interpretation and replace the existing provisions on excess computer time.

H. By-Products

The sale of by-products of the development of a program for a permissible data processing activity is currently treated in the Board's data processing interpretation as a permissible incidental activity.[16] By-products may be data, software, or data processing techniques or information developed by the bank holding company. The proposed amendment would add a provision to the regulation stating that providing by-products of permissible data processing and transmission services is closely related to banking. Relying on the Board's previous determination that the sale of by-products is an incidental acitivity to permissible data processing, the Administrative Law Judge recommended that Regulation Y be amended to include the sale of any by-products of permissible data processing and transmission activities, so long as the by-products are not designed or appreciably enhanced for the purpose of marketability.

The Board believes the record supports adoption of the Administrative Law Judge's recommendation, but that it is appropriate to continue to treat the sale of by-products in its data processing interpretation as an incidental activity. Accordingly, the by-products provision of the data processing interpretation is revised to incorporate the provisions of the recommended amendment.

I. The Requirement of Separate Bookkeeping

The Administrative Law Judge recommended that the Board include in Regulation Y a separate bookkeeping provision that was not contained in the proposed regulation. Under this recommended provision, where permissible data processing and data transmission activities are provided by a bank holding company subsidiary or related entity, the entity providing the services will have separate books and financial statements and provide these documents to any new or renewal customer who requests financial information.

The Board finds that the recommended provision is appropriate but should not be included as a part of Regulation Y. Section 4(c)(8) of the Bank Holding Company Act requires the Board, in authorizing nonbank activities for bank holding companies, to make two separate determinations. First, the Board must determine that the activity is closely related to banking. Second, the Board must determine whether the public benefits expected from a particular activity outweigh any possible adverse effects, such as unfair competition. In making the closely related to banking finding, the Board may proceed by order or regulation; however, the Board resolves the "public benefits" test on a case-by-case basis. Section 225.4 of Regulation Y designates the nonbanking activities the Board has determined meet the statutory test of being closely related to banking.

The record of this proceeding does not show that the Administrative Law Judge's recommended separate books requirement has any bearing on a determination that the proposed activities are closely related to banking and, accordingly, such a requirement is inappropriate for inclusion in the regulation. However, the Board believes that such a requirement is appropriate to minimize any dangers of adverse competitive effects. Therefore, the Board has determined to include a separate books and financial statements requirement in the revision of its data processing interpretation.

III. Public Comments on the Proposal

The Board received sixty-three comments on the proposed rule, of which thirty-five favored the proposal. The favorable comments, most of which were from banking organizations, asserted that the proposed rule merely reflects the technological developments in the data processing field in the past decade. The commentors also asserted that the services proposed to be provided under the proposed rule are services that banks have always provided to their customers. A few of the favorable comments suggested that the banking industry's involvement in data processing will mean greater innovation and access to the special expertise of banks in financial matters.

Twenty-five comments opposed the

[14] These include systems software (*i.e.*, software designed only to control and operate the hardware, not to perform substantive operations), network communications support, and the operating personnel and documentation necessary for the maintenance and use of these facilities.

[15] The *National Courier* court determined that activities that are necessary to the performance of closely related activities are incidental to closely related activities. 516 F.2d at 1241.

[16] Footnote 13, *supra*.

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proposal, of which twenty-one were from data processing organizations. In addition to generally asserting that the expanded data processing and data transmission activities are not closely related to banking, these data processing organizations asserted that entry of bank holding companies into the field would drive them out of business. These commentors also made four specific assertions concerning adverse effects on competition that would result if bank holding companies were permitted to offer the proposed services. These effects are tying, cross-subsidization, manipulation of the stock of data processing companies that banks hold in their portfolios and improper financial leverage.

With the exception of comments concerning the closely relatedness to banking of the proposed services, which are discussed above, the unfavorable comments from the data processing organizations concern adverse competitive effects that may result if bank holding companies engage in the proposed activities. These considerations relate to the public benefits test and, as explained above, the Board must consider the likelihood of the type of anticompetitive consequences raised by the comments with respect to each proposal by a bank holding company to engage in permissible data processing activities.

In addition, the record in this proceeding contains evidence relating to the effect of expanded bank holding company participation in the data processing industry generally and the Administrative Law Judge made explicit findings, which the Board adopts, that expansion of bank holding company data processing activities, as a general matter, is not likely to result in decreased competition, voluntary tying, cross-subsidization or predatory pricing, or undue concentration of resources. These findings, which were based primarily on the highly decentralized structure of the data processing services industry, support the Board's determination that the activities encompassed by the proposed amendment are permissible and appropriate for bank holding companies.

With regard to manipulation of stock and improper financial leverage, the unfavorable commentors provided no indication of exactly what these effects consist of and no evidence that bank holding companies have or are likely to engage in these practices. The Board regards the commentors concerns in this regard to be merely speculative and determines that these comments do not require the Board to disapprove the proposed amendment.

Several banking organizations opposed the amendment asserting that certain aspects of the proposed rule represent a method to circumvent the restrictions on interstate banking. One commentor also stated that the home banking portions of the proposed rule are in conflict with the Electronic Funds Transfer Act, 15 U.S.C. 1601 *et seq.*, the Board's Regulation E, 12 CFR Part 205, and other consumer credit laws.[17]

However, no evidence has been presented that the approved activities would necessarily violate these restrictions or that such activities could not be conducted in compliance with the restrictions against interstate banking or with Regulation E under any circumstances. The Board expects that a bank holding company that has received Board approval to engage in data processing and transmission services covered by the amended regulation will comply with all applicable legal requirements. These considerations do not therefore warrant a decision not to adopt the amendment to Regulation Y.

IV. Regulatory Flexibility Act

The Small Business Administration submitted an opinion that the Regulatory Flexibility Act, 5 U.S.C. 601 *et seq.*, required the preparation of an initial flexibility analysis in conjunction with the notice of proposed rulemaking. The Administrative Law Judge determined that the Regulatory Flexibility Act did not apply to the proposed rule because the initial notice of proposed rulemaking was published before the effective date of that Act.

The Board believes that it is unnecessary to determine whether this rulemaking proceeding preceded the effective date of the Regulatory Flexibility Act. Under section 605(b) of that Act, 5 U.S.C. 605(b), the Act's provisions requiring the preparation of an initial or final flexibility analysis do not apply to any proposed or final rule if the head of the agency certifies that the rule, if promulgated, will not have a significant economic impact on a substantial number of small entities.

[17] The comment stated that Regulation E requires written documentation of certain electronic funds transfers and home banking terminals currently in use do not provide such documentation.

This amendment clarifies and expands the types of data processing and transmission services that may be engaged in by a bank holding company or its nonbank subsidiaries. As the Administrative Law Judge found, the amendment does not impose any recordkeeping, reporting, or compliance requirement on any entities, including small entities.[18]

Therefore, pursuant to section 605(b) of the Regulatory Flexibility Act, 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.

List of Subjects in 12 CFR Part 225

Banks, banking, Holding companies.

Accordingly, pursuant to its authority under sections 4(c)(8), and 5(b) of the Bank Holding Company Act, 12 U.S.C. 1843(c)(8), and 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

I. Section 225.4 amended by revising paragraph (a)(8) to read as follows:

§ 225.4 Nonbanking activities.

(a) * * *

(8)(i) Providing data processing and data transmission services, data bases or facilities (including data processing and data transmission hardware, software, documentation and operating personnel) for the internal operations of the holding company or its subsidiaries;

(ii) Providing to others data processing and transmission services, facilities,

[18] The Small Business Administration, supported by Protestants, asserts that the amendment will have a substantial economic effect on nonbank data processing service organizations, many of which are small entities, by permitting large banking organizations, such as Citicorp, to compete with such organizations. A review of the terms, purpose and legislative history of the Regulatory Flexibility Act demonstrates, however, that by applying the Act to a rule with significant economic impact on small entities, Congress meant regulations that directly impose federal recordkeeping, compliance and reporting requirements that may result in potentially unnecessary legal, accounting, and consulting costs on institutions with limited resources. *See* 94 Stat. 1164. The amendment adopted by the Board imposes no such regulatory or reporting requirements.

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