

SCHWARTZ & BALLEN
1990 M STREET, N.W. · SUITE 500
WASHINGTON, DC 20036-3418

(202) 776-0700

FACSIMILE
(202) 776-0720

M E M O R A N D U M

March 14, 2000

To: Our Clients and Friends

Re: Federal Reserve Action on Activities of Financial Holding Companies

The Federal Reserve Board has adopted three interim rules to facilitate bank holding companies that intend to become financial holding companies and state member banks that wish to establish subsidiaries to engage in financial activities under the Gramm-Leach-Bliley Act (the “GLB Act”).

- The first rule specifies what activities constitute “financial activities” under the GLB Act.
- The second rule imposes two operating standards on financial holding companies that establish securities affiliates.
- The third rule permits state member banks to establish financial subsidiaries and engage in financial activities.

The three rules can be found on the Federal Reserve’s website at <http://www.bog.frb.fed.us/>.

The Federal Reserve is seeking comment on these rules until May 12th.

Financial Activities

The Federal Reserve has amended Regulation Y to identify the financial activities that financial holding companies may engage in under the GLB Act.

SCHWARTZ & BALLEN

- This list also determines what companies will be subject to the privacy provisions of Title V of the GLB Act.
- The rule includes all the activities which the Board currently has authorized bank holding companies to engage in by regulation and order under Section 4(c)(8) of the Bank Holding Company Act as well as those activities that Congress specified as “financial” in the GLB Act.
- The rule establishes the process to follow in order to request the Federal Reserve to add activities to the list of financial activities, as well as how to determine whether activities are “incidental” or “complementary” to financial activities.
- The rule requires a financial holding company to file a notice with the appropriate Reserve Bank within 30 days after it has begun engaging in financial activities. The notice must describe the activities engaged in and the identity of the companies which engage in the activities.
- A financial holding company may acquire a company that engages in some impermissible activities if it commits to terminate or divest the impermissible activities within two years. The company engaged in impermissible activities may not engage in or acquire a company engaged in any activity that is not a financial activity.
- While a financial holding company may organize, sponsor and manage mutual funds, it may not own more than 25 percent of the equity of a fund after one year.

The Federal Reserve notes that new activities engaged in by financial holding companies are to be conducted in accordance with the laws of the jurisdiction in which the activity is conducted. In addition, the Federal Reserve reserves the right to require prior notice and prior approval under certain supervisory circumstances.

Securities Affiliate Operating Standards

The Board has exercised its authority under the GLB Act to impose prudential limitations on relationships between depository institutions and their securities affiliates.

SCHWARTZ & BALLEN

- Intra-day extensions of credit to a securities affiliate from an affiliated bank or thrift institution must be on market terms consistent with Section 23B of the Federal Reserve Act.
- U.S. branches and agencies of foreign banks that are financial holding companies must abide by the limitations of Sections 23A and 23B when lending to, or purchasing assets from, securities affiliates.

State Member Banks' Formation of Financial Subsidiaries

The GLB Act authorizes state member banks to establish financial subsidiaries to engage in financial activities. The Federal Reserve's rule specifies procedures for a state member bank to follow to establish financial subsidiaries. The rule includes remedial procedures in the event a state member bank fails to meet the capital, management or CRA requirements of the GLB Act.

If you have any questions concerning these rules, please call Gilbert Schwartz, Robert Ballen or Tom Fox at 202-776-0700.