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Federal Reserve permits holding companies to engage in some non-banking activities

By Julie Randall

Bank holding companies may, for a variety of reasons, add non-banking activities to their operations. The Bank Holding Company Act of 1956, as amended, limits the types of non-banking activities in which BHCs can engage; however, there are some non-banking activities that BHCs may engage in, directly or indirectly through a subsidiary. Many of these require the prior approval of the Federal Reserve, while others may be conducted without obtaining prior approval. In this article, I will discuss the more common activities that BHCs can perform that do not require prior approval. I will also discuss the limitations and restrictions that apply to activities about which we frequently receive questions. Later this year, we'll discuss activities that require prior approval.

The BHC Act identifies activities a BHC may provide without obtaining prior approval. Generally, these activities involve providing a service to the subsidiary bank(s) and include:

- Holding or operating properties used wholly or substantially by any banking subsidiary of the BHC in the operations of such banking subsidiary or acquired for such future use;
- Conducting a safe deposit business;
- Furnishing services to or performing services for the BHC or its banking subsidiaries; or
- Liquidating assets acquired from the BHC or its banking subsidiaries.

Regulation Y further defines the servicing activities referenced in the BHC Act and lists other non-banking activities that do not require the Federal Reserve's prior approval as well. Servicing activities as defined in Regulation Y include, but are not limited, to activities below:

- Accounting, auditing and appraising;
- Advertising and public relations;
- Data processing and data transmission services, data bases and facilities;
- Personnel services;
- Courier services;

- Holding or operating property used wholly or substantially by a subsidiary in its operations or for its future use;
- Liquidating property acquired from a subsidiary; and
- Selling, purchasing or underwriting insurance, such as blanket bond insurance, group insurance for employees, and property and casualty insurance.

BHCs must report these activities by submitting an FR Y-10 to the appropriate Reserve Bank when they begin conducting them. BHCs also need to appropriately compensate their bank subsidiaries for any resources that subsidiaries may provide in association with the activities (e.g., personnel).

We frequently get questions regarding two of these activities: holding of real estate and acquiring assets for liquidation. BHCs can hold real estate that is or will be in the future, premises for a bank subsidiary. However, the phrase “used wholly or substantially” is key since unused space the BHC might lease to third parties could raise concerns if it represents a significant proportion of the property. The Federal Reserve makes the determinations based on the facts and circumstances of particular situations; we have not defined the term “substantially.” Generally, if the BHC does not propose to use 25 percent or more of the property for banking operations upon acquisition or increase its use to 50 percent in a reasonably short period of time, it should consult with the Federal Reserve prior to acquiring the property.

BHCs can acquire other real estate and loans from their bank subsidiaries for the purposes of liquidation; however, certain restrictions apply to activities conducted under the servicing exemption. If the BHC acquires other real estate, it must intend to sell the property as soon as feasible. It cannot extend any credit in association with its holding of the property, and it can invest in the property only to the extent necessary to ensure its marketability to potential buyers. In other words, the BHC cannot treat the property as if it were a business the company would continue to operate. If the BHC acquires a loan, it cannot alter the loan’s terms or conditions since this would represent a new loan to the entity, and the BHCA would be engaging in lending activities rather than liquidating an asset. BHCs also need to ensure their purchases of the loans or other real estate from their bank subsidiaries comply with the market value requirement of section 23B of the Federal Reserve Act.

The discussion above highlights only a few of the non-banking activities that do not require the Federal Reserve’s prior approval. If you have questions about the permissibility of a non-banking activity or whether it would qualify of a servicing exemption, please contact Reserve Bank staff to discuss the proposed transaction.

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