OVERVIEW OF THE GRAMM – LEACH - BLILEY ACT

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This document was prepared by the Federal Reserve Bank of Cleveland's Supervision and Regulation staff for use in general discussions about the Gramm-Leach-Bliley Act. The views expressed herein are those of the authors and are not necessarily those of the Federal Reserve Bank of Cleveland or the Board of Governors of the Federal Reserve System. This document should not be construed as legal advice on any specific matter. Readers are urged to consult legal counsel before making decisions related to the Gramm-Leach-Bliley Act. Specific regulatory questions may be addressed to the persons identified in the Contacts section on page 17.

Overview of the Gramm-Leach-Bliley Act

The Gramm-Leach-Bliley Act of 1999 facilitates affiliations between banks and securities firms by repealing sections 20 and 32 of the Glass-Steagall Act. It also authorizes bank holding companies and foreign banks[1] that meet eligibility criteria to become financial holding companies, thus allowing them to engage in a broad array of financially related activities. In addition, the act provides for the functional regulation of financial holding companies, protects nonpublic customer information held by financial institutions, alters supervision related to the Community Reinvestment Act, and makes other regulatory changes.

To become a financial holding company, a bank holding company must file a declaration with the appropriate Federal Reserve Bank and with the Board of Governors of the Federal Reserve System certifying that *all* of its depository institution subsidiaries are well capitalized and well managed. Declarations to become a financial holding company are not effective unless *all* of the bank holding company's insured depository institution subsidiaries are rated "satisfactory" or better under the Community Reinvestment Act.[2]

Expanded Powers for Financial Holding Companies

The Gramm-Leach-Bliley Act adds section 4(k) to the Bank Holding Company Act, authorizing financial holding companies to engage in a broad array of activities (referred to here as "4(k) activities").

Financially Related Activities. The act authorizes financial holding companies to engage in activities that are financial in nature, including:

- Securities underwriting and dealing
- Insurance agency and underwriting activities
- Merchant banking activities.

Other Financial Activities. Financial holding companies may engage in any other activity that the Federal Reserve Board—after consultation with the Secretary of the Treasury—determines to be financial in nature or incidental to financial activities. Other financial activities encompass three areas:

- Lending, exchanging, transferring, investing for others, or safeguarding financial assets other than money or securities
- Providing any device or other instrumentality for transferring money or other financial assets
- Arranging, effecting, or facilitating financial transactions for the account of third parties.

The Federal Reserve Board and the Treasury Secretary have determined that acting as a finder is incidental to financial activity and, therefore, is permissible for financial holding companies. Finders may (among other things) host an internet marketplace consisting of links to the Web sites of buyers and sellers. Finders may also operate Web sites allowing buyers and sellers to post information concerning products and services and to enter into transactions among themselves.

Complementary Activities. Financial holding companies may engage in any nonfinancial activity that the Federal Reserve Board determines is complementary to financial activity *and* does not pose substantial risk to the safety or soundness of depository institutions or to the financial system.

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[1] This document does not summarize provisions of the act dealing with foreign banks. However, foreign banks operating in the United States must meet criteria similar to those for bank holding companies to file a declaration to become a financial holding company. See "Procedures to Become a Financial Holding Company and Guidance Regarding the Initial Monitoring of Acquisitions and the Commencement of New Activities by Financial Holding Companies," SR Letter 00-1, February 8, 2000, for guidance.

[2] The Federal Reserve has issued final regulations and guidance dealing with declarations to become financial holding companies; see 66 F.R. 400, January 3, 2001, and SR Letter 00-1, February 8, 2000.

Generally, financial holding companies do not need Federal Reserve Board approval to engage in or acquire companies engaged in activities that are financial in nature. However, financial holding companies must provide written notice to the Federal Reserve Board within 30 days of commencing the activity or acquiring the entity that engages in the activity.[3] Prior Federal Reserve Board approval is required for financial holding companies to acquire control of a bank or savings and loan association or to engage in any complementary activity. Bank holding companies (that have not elected to become financial holding companies) may engage only in activities that the Federal Reserve Board has determined to be closely related to banking under section 4©(8) of the Bank Holding Company Act.

Regulatory Actions. On December 21, 2000, the Federal Reserve Board approved a final rule listing the financial activities that are permissible for financial holding companies. The rule also established a procedure by which financial holding companies may seek a Federal Reserve Board determination that a particular activity is complementary to financial activity and receive approval to engage in that activity.[4]

The Federal Reserve Board and the Secretary of the Treasury issued a final rule implementing the merchant banking provisions of the act on January 10, 2001.[5] The final rule limits financial holding companies' exposure to merchant banking investments. In addition, on January 18, 2001, the Federal Reserve Board, Office of the Comptroller of the Currency (OCC), and Federal Deposit Insurance Corporation (FDIC) proposed a rule that would impose additional capital requirements on merchant banking and similar investments on a sliding scale, with a maximum capital charge of 25 percent.[6]

The Federal Reserve Board issued a proposal for comment to change the conditions governing the conduct of financial data processing activities—which were previously found to be closely related to banking—to allow a greater amount of nonfinancial data processing in connection with financial data processing. The proposal would also allow financial holding companies, as activities complementary to financial activities, to own companies engaged in certain types of data storage, internet, portal housing, and advisory activities involving data processing.[7] The Federal Reserve Board has sought comment on whether it should permit financial holding companies to invest in companies that engage in new technology, communications, and e-commerce activities.

The Federal Reserve Board issued a proposal for comment on whether to determine that real estate brokerage and real estate management are financial in nature or incidental to financial activity, and therefore permissible for financial holding companies or financial subsidiaries of state member banks.[8] In making such a determination, the Gramm-Leach-Bliley Act instructs the Federal Reserve Board and the Secretary of the Treasury to consider whether the activity is necessary or appropriate to allow financial holding companies or banks to effectively compete with other domestic financial services companies.

Expanded Powers for Banks

The Gramm-Leach-Bliley Act authorizes a number of activities for banks and their subsidiaries.

Municipal Revenue Bonds. Well-capitalized national banks may directly underwrite and deal in municipal revenue bonds. Because of existing provisions of the Federal Reserve Act and the Federal Deposit Insurance Act, this authority also extends to state banks.

[3] If prior Federal Reserve Board approval is not required in connection with the acquisition of a nonbanking company, financial holding companies should determine whether they must file with the Federal Trade Commission pursuant to the Hart-Scott-Rodino Act; see Formal Interpretation No. 17, 65 F.R. 17880, April 5, 2000.
[4] See 66 F.R. 400, January 3, 2001.
[5] See 66 F.R. 8465, January 31, 2001, and SR 00-09, June 22, 2000.
[6] See 66 F.R. 10212, February 14, 2001.
[7] See 65 F.R. 80384, December 21, 2000.
[8] See 66 F.R. 307, January 3, 2001.

National Bank Financial Subsidiaries. The act authorizes national banks to own or control a "financial subsidiary" that engages, as principal or agent, in activities that are not directly permissible for national banks. To do so, the bank and its financial subsidiary must meet certain criteria and must comply with certain conditions involving permissible activities, financial and managerial status of the bank and its affiliates, CRA rating, issuance of subordinated debt, investment limitations, capital deduction, financial statement disclosure, affiliate transactions, and financial and operational safeguards.

- Generally, a financial subsidiary may not engage as principal in underwriting insurance, providing or issuing annuities, real estate development or investment, or merchant banking activities.
- Complementary activities are not authorized for financial subsidiaries of national banks.
- Prior OCC approval is required for national banks to conduct activities through a financial subsidiary.

State Member Bank Subsidiaries. State member banks may own or control subsidiaries that engage as principal in activities that national banks may conduct through financial subsidiaries, if the bank and its subsidiary comply with the conditions and limitations that apply to national banks.

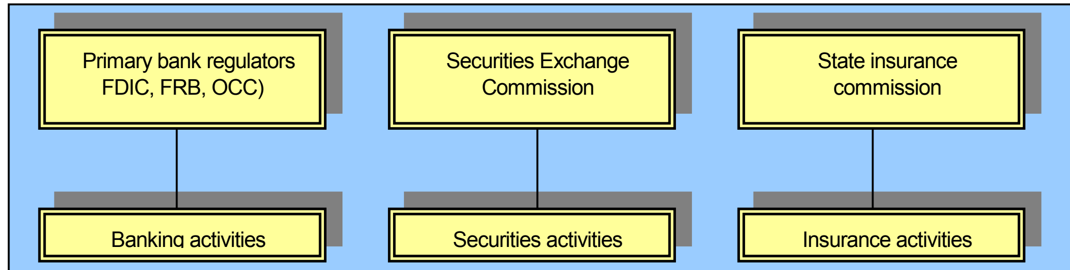
Section 24. Because the Gramm-Leach-Bliley Act does not alter section 24 of the Federal Deposit Insurance Act, state banks may still engage as principal in activities that are not permissible for national banks, if the FDIC determines the activity poses no significant risk to the deposit insurance fund and if the state bank is in compliance with applicable capital standards.

Regulatory Actions. The Federal Reserve Board and the OCC issued interim rules for financial subsidiaries of state member banks and national banks on March 10, 2000.[9] The rules describe the types of activities that are permissible for financial subsidiaries and list the qualifications that national banks must satisfy to hold an interest in a financial subsidiary. Additionally, the rules establish a streamlined notice procedure for state member banks wishing to engage in financial activities through a financial subsidiary.

The Federal Reserve Board also issued supervisory guidance to state member banks related to underwriting, dealing in, and investing in municipal revenue bonds.[10]

9 See 65 F.R. 14810, March 20, 2000.
10 See SR 01-13, May 14, 2001.

Supervision



The Federal Reserve Board serves as the “umbrella” supervisor of all bank holding companies—including financial holding companies—and it has the authority to require reports from and examine any bank holding company (including financial holding companies) and any subsidiary. However, the act places certain limits on supervisory powers with respect to functionally regulated subsidiaries of bank holding companies.[11] The Federal Reserve Board must, to the fullest extent possible, rely on examination reports prepared by the subsidiary’s functional regulator. In addition, the Federal Reserve Board may examine functionally regulated subsidiaries *only if* it reasonably believes any of the following:

- The subsidiary is engaged in activities that pose a material risk to an affiliated depository institution.
- Examination of the subsidiary is necessary to adequately inform the Federal Reserve Board about the holding company’s systems for monitoring and controlling financial and operational risks.
- The subsidiary is not in compliance with the Bank Holding Company Act or any other federal law that the Federal Reserve Board has specific jurisdiction to enforce against the subsidiary, and the compliance determination cannot be made through an examination of the financial holding company or an affiliated depository institution.

The Federal Reserve Board is generally prohibited from imposing capital requirements on functionally regulated subsidiaries that are in compliance with federal and state requirements. In addition, the Federal Reserve Board may not require certain functionally regulated subsidiaries to provide funds or assets to affiliated depository institutions, except in very limited circumstances. Finally, the act authorizes banking regulators to adopt prudential standards and restrictions on relationships or transactions between depository institutions and their subsidiaries and affiliates.

Insurance Activities

The Gramm-Leach-Bliley Act contains a number of provisions dealing with the insurance activities of financial holding companies and bank subsidiaries. The act affirms the states’ role in regulating insurance activities, including those of financial subsidiaries of banks and insurance companies affiliated with financial holding companies. However, the act also preempts certain state laws.

Financial Holding Company Affiliates. Nonbank affiliates of financial holding companies may engage in insurance underwriting and agency activities, as discussed in “Expanded Powers for Financial Holding Companies” on page 1.

Place of 5,000. National banks may continue to engage in insurance agency activities from a place with a population of 5,000 or less.

Financial Subsidiaries. National banks may engage in insurance agency activities through a financial subsidiary at any location, subject to the criteria and conditions discussed in “Expanded Powers for Banks” on page 2.

11 See section 111 of the Gramm-Leach-Bliley Act and SR 00-13, August 15, 2000.

Title Insurance. National banks that are not currently engaged in the underwriting or sale of title insurance are prohibited from commencing that activity. However, sales activities by banks are permitted in states that specifically authorize such sales for state banks, subject to the same conditions. National bank subsidiaries are permitted to sell all types of insurance, including title insurance.

Preemption of State Anti-Affiliation Laws. The act preempts any state law that prevents or significantly interferes with affiliations authorized or permitted by the federal law between depository institutions or an affiliate thereof and insurance entities.

Preemption of Other State Laws. The act preempts any state law that prevents or significantly interferes with the insurance sales, solicitation, or cross-marketing activities of any insured depository institution or affiliate thereof, except for state laws that fit certain "safe harbor" provisions or that meet the act's nondiscrimination standard.

Regulatory Actions. Consumer protection regulations that apply to retail sales practices, solicitations, advertising, or offers of any insurance product by a depository institution or any person that is engaged in such activities at an office of the institution or on behalf of the institution became effective October 1, 2001.[12]

Bank Securities Activities

The Gramm-Leach-Bliley Act makes a number of changes to the regulation of bank securities powers.

Financial Holding Company Affiliates. Nonbank affiliates of financial holding companies may engage in securities underwriting and agency activities, as discussed in "Expanded Powers for Financial Holding Companies" on page 1.

Financial Subsidiaries. National banks may engage in securities underwriting activities through financial subsidiaries, subject to the criteria and conditions discussed in "Expanded Powers for Banks" on page 2.

Broker/Dealer Exemption. The act repeals the bank exemption from the definitions of "broker" and "dealer" in the securities laws and substitutes narrower exemptions for traditional bank securities activities such as transactions related to trust operations, government securities, and third-party networking arrangements

Investment Advisor Exemption. The act repeals the bank exemption from registration as an investment advisor under the Investment Advisors Act (effective May 12, 2000).

Mutual Fund Distribution. By repealing section 32 of the Glass-Steagall Act, the Gramm-Leach-Bliley Act gives member banks the authority to act as distributors for mutual funds.

Regulatory Actions. The SEC adopted an interim final rule that replaces banks' general exemption from the terms "broker" and "dealer" with 15 specific exceptions.[13] The rule had been scheduled to become effective October 1, 2001; however, the Federal Reserve Board, FDIC, and OCC asked the SEC to delay that date.[14] The SEC has delayed the effective date until May 12, 2002.[15]

[12] See 65 F.R. 75822, December 4, 2000, and 66 F.R. 15345, March 19, 2001.
[13] See 66 F.R. 27759, May 18, 2001.
[14] See the Federal Reserve Board's press release dated July 2, 2001.
[15] See 66 F.R. 38370, July 24, 2001.

Privacy

The Gramm-Leach-Bliley Act contains a number of new requirements related to customer financial information.

Disclosure of Information-Sharing Policies and Procedures. The act requires financial institutions[16] to provide clear and conspicuous notice to consumers—prior to establishing a customer relationship and at least annually thereafter—of the institution's policies and practices regarding the collection and disclosure of nonpublic personal information to affiliates and third parties.

"Opting Out" of Information-Sharing Arrangements with Third Parties. The act prohibits financial institutions from disclosing nonpublic personal information to nonaffiliated third parties, unless the institution informs the consumer that such information may be shared with third parties *and* allows the consumer to "opt out" of such sharing arrangements.

Prohibition on Disclosing Account Numbers for Marketing Purposes. Financial institutions are generally prohibited from disclosing customers' account numbers or access codes for deposit, transaction, or credit card accounts to nonaffiliated third parties for use in marketing programs, including telemarketing and direct mail programs.

Prohibition on Obtaining Financial Information under False Pretenses. The act prohibits most persons from obtaining customer information from a financial institution[17] or from a customer of a financial institution through the use of false, fictitious, or fraudulent statements or representations.

The act sets forth a number of general exceptions to the disclosure and opt-out provisions, including exceptions related to the disclosure of information to service providers and joint marketing partners. Federal regulators have issued proposed rules for comment implementing the privacy provisions.[18]

Regulatory Actions. On May 10, 2000, the federal bank regulatory agencies approved final regulations to implement the act's consumer privacy provisions.[19] The regulations limit financial institutions' disclosure of "nonpublic personal information" about individuals who obtain financial products or services for personal, family, or household purposes. Subject to certain exceptions allowed by the law, the regulations cover information sharing between financial institutions and nonaffiliated third parties. The final regulations require financial institutions to provide initial notices to customers about their privacy policies; to provide annual notices of their privacy policies to their current customers; and to provide a reasonable method for consumers to opt out of disclosures to nonaffiliated third parties. Consumers may exercise their opt-out option at any time. The regulation became effective November 13, 2000, but full compliance was optional until July 1, 2001.

On February 2, 2001, the federal bank regulatory agencies published final regulations establishing standards for safeguarding customer information.[20]

On March 27, 2001, the federal bank and thrift regulatory agencies issued rules to implement the Fair Credit Reporting Act's notice and opt-out provisions, which govern information sharing among financial institution affiliates.[21]

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[16] For the purposes of this provision, the term "financial institution" refers to any company (regardless of whether it is affiliated with a bank) that engages in financial activities that are permissible for financial holding companies.

[17] For the purposes of this prohibition, the term "financial institution" includes depository institutions, securities broker-dealers, insurance companies, loan and finance companies, credit card issuers and networks, and consumer reporting agencies. This definition may also include any entity that the Federal Trade Commission determines is providing financial services to consumers.

[18] See 65 F.R. 8770, February 22, 2000.

[19] See 65 F.R. 35162, June 1, 2000.

[20] See 66 F.R. 8616, February 1, 2001, and SR 01-15, May 31, 2001.

[21] See 66 F.R. 16624, March 27, 2001.

On April 26, 2001, the Federal Reserve Board issued guidance on the protection of customer information against identity theft and pretext calling.[22]

On June 4, 2001, the Federal Reserve Bank of Cleveland distributed Regulation P examination procedures to regulated institutions.[23]

CRA Provisions

Sunshine Provisions. The Gramm-Leach-Bliley Act requires each party to a covered CRA-related agreement to fully disclose the agreement and its terms to the public and to the appropriate federal banking agency for the insured depository institution involved in the agreement. Each party to a covered CRA-related agreement must submit an annual report to the appropriate federal banking agency concerning the use of CRA-related money and resources during the previous year.

Examination Cycle. Under the act, any insured depository institution with aggregate assets under $250 million is subject to routine CRA examinations on a five-year cycle if the institution received an “outstanding” rating at its most recent CRA examination, or on a four-year cycle if the institution received a “satisfactory” rating at its most recent CRA examination.

The federal banking agencies may conduct nonroutine examinations for reasonable cause in such circumstances, as they deem appropriate. Other than the changes indicated above, CRA examination cycles remain unchanged.

Regulatory Actions**.** On December 21, 2000, the federal regulatory agencies issued a final rule implementing the CRA Sunshine requirements.[24] The rule establishes annual reporting and public-disclosure requirements for certain written agreements between insured depository institutions or their affiliates and nongovernmental entities or persons made pursuant to, or in connection with, the fulfillment of the CRA. The rule identifies the types of written agreements covered by the act and defines many of the terms used in the statute. The rule also describes how parties to a covered agreement must make the agreement available to the public and the appropriate agencies, and it explains the type of information that must be included in the annual report filed by parties to a covered agreement.

Other Significant Aspects

Transactions with Affiliates. The Gramm-Leach-Bliley Act requires the Federal Reserve Board to adopt rules under section 23A of the Federal Reserve Act to address credit exposure arising from derivative transactions between member banks and their affiliates and intraday extensions of credit by member banks to their affiliates. In addition, covered transactions between banks and their financial subsidiaries are subject to a 20 percent quantitative limit and the collateral requirements of section 23A. Furthermore, the act presumes that covered transactions between depository institutions and certain companies—such as financial holding company affiliates that engage in merchant banking activities—are subject to the limitations and requirements of section 23A.

Regulatory Actions. On May 4, 2001, the Federal Reserve Board issued interim rules requiring the adoption of policies and procedures to monitor, manage, and control credit exposures arising from derivative transactions with affiliates and intraday credit extensions to affiliates, as well as subjecting them to the market-terms requirements of section 23B. The rule has a delayed effective date of January 1, 2002.[25] In addition, the Federal Reserve Board issued proposed Regulation W for comment, which compiles previous interpretations and provides new interpretations of sections 23A and 23B.[26]

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[22] See SR 01-11, April 26, 2001.
[23] See Circular Letter 01-49, June 4, 2001.
[24] See 66 F.R. 2051, January 10, 2001, and the correction in 66 F.R. 14071, March 9, 2001.
[25] See 66 F.R. 24229, May 11, 2001.
[26] See 66 F.R. 24186, May 11, 2001.

Unitary Thrift Holding Companies. Companies that file applications with the Office of Thrift Supervision (OTS) to acquire a thrift after the grandfather date (May 4, 1999) may only engage in activities that are permissible for financial holding companies. Existing unitary thrift holding companies are grandfathered and may continue to engage in any type of financial or commercial activity.

Federal Home Loan Bank System. The act allows insured depository institutions with assets under $500 million to become members of the Federal Home Loan Bank System without satisfying the "qualified thrift lender" test. The act also authorizes the Federal Home Loan Bank System to make long-term advances to insured depository institution with assets under $500 million that are secured by loans to small businesses, small farms, and small agribusinesses.

Disclosure of ATM Surcharges. The act requires that ATM operators imposing surcharges to post a notice that surcharges may be imposed and to inform the consumer, through an on-screen message or paper receipt, of the amount of the surcharge before the consumer commits to completing the transaction.

Regulatory Actions. Regulation E, which implements the Electronic Funds Transfer Act, was revised to reflect the Gramm-Leach-Bliley Act's requirement for notification for ATM surcharges. This rule became effective March 9, 2001; however, to provide adequate time to make any necessary systems changes, the mandatory compliance date was delayed until October 1, 2001.[27]

[27] 66 F.R. 13409, March 6, 2001.

Questions and Answers

Detailed below are questions and answers that Federal Reserve Bank of Cleveland staff have received since the legislation was enacted. Please consult your legal counsel before making decisions related to the Gramm-Leach-Bliley Act.

Financial Holding Company Declarations

Should a bank holding company become a financial holding company?

The decision to become a financial holding company depends on the company's strategic business plan, capital position and projections, management strength, risk-management systems, expected debt ratings, and accounting and tax consequences. Becoming a financial holding company is ultimately the decision of senior management and the board of directors.

While financial holding company status allows bank holding companies to engage in a wide variety of financial and complementary activities, failure to maintain financial holding company criteria could significantly affect the company's strategic business plan. Refer to the "Supervision" section on page 11 for restrictions placed on bank holding companies that have requested financial holding company status and failed to maintain the applicable criteria. If the organization does not have immediate plans to engage in financially related activities, the bank holding company may want to delay submitting a declaration.

How can a domestic bank holding company apply to become a financial holding company?

Once senior management and the directorate have made the decision to apply for financial holding company status, domestic bank holding companies must file a written declaration with the appropriate Reserve Bank. The declaration must contain the following information:

- Statement that the bank holding company elects to become a financial holding company
- Name and head office address of the company and each depository institution controlled by the company
- Certification that all depository institutions controlled by the company are well capitalized as of the filing date
- Capital ratios for all relevant capital measures (defined in section 38 of the Federal Deposit Insurance Act), as of the close of the previous quarter, for each depository institution controlled by the company on the filing date
- Certification that all depository institutions controlled by the company are well managed as of the filing date.[28] A depository institution is considered "well managed" if it has received at least a satisfactory composite rating for safety and soundness *and* at least a satisfactory rating for management. Or, if the depository institution has not received an examination rating, by determination of the Federal Reserve Board.

The declaration must be signed by an official or a representative with the authority to bind the company. Although it is not required to be included within the declaration, all insured depository institutions controlled by the bank holding company as of the filing date must have a satisfactory or better CRA rating for the declaration to be effective. Declarations should be sent to:

Federal Reserve Bank of Cleveland
Cindy West, Banking Supervisor
Supervision and Regulation Department
P.O. Box 6387
Cleveland, Ohio 44101

[28] See 12 C.F.R § 225.82, and SR 00-1, February 8, 2000.

When do financial holding company declarations become effective?

Declarations become effective on the thirty-first day after the date the declaration was received by the Federal Reserve Bank, unless the company is notified otherwise. However, the Federal Reserve Board may affirmatively notify a company that its declaration is effective prior to the expiration of 30 days.

The Federal Reserve Board has 30 days from the receipt of the declaration to notify a bank holding company that its request is ineffective. The Federal Reserve Board may find the election to be ineffective if any of the depository institutions controlled by the bank holding company are not well capitalized, well managed, or have a less-than-satisfactory CRA rating.[29]

How does the Gramm-Leach-Bliley Act affect bank holding companies that do not elect to become financial holding companies?

Permissible nonbanking activities remain the same for bank holding companies that do not elect to become financial holding companies. Bank holding companies are limited to engaging in activities that the Federal Reserve Board has determined to be closely related to banking under section 4c(8) of the Bank Holding Company Act.[30]

Supervision: Cure Provisions

What are the consequences for financial holding companies whose depository institution subsidiaries cease to meet capital or management requirements?

The Federal Reserve Board will notify the financial holding company in writing upon discovering that not all depository institutions controlled by the company are well capitalized or well managed. There may be occasions when a financial holding company is aware that one of its subsidiaries has ceased to be well capitalized or well managed before the Federal Reserve Board has access to such data. Under such circumstances, financial holding companies are required to notify the Federal Reserve Board immediately of the institutions involved and the areas of noncompliance.

Within 45 days of receiving a noncompliance notice, the financial holding company must execute an agreement with the Federal Reserve Board to comply with the applicable capital and management requirements. The agreement must explain the actions the company will take to correct each deficiency; provide a schedule detailing when each action will be taken; provide any other information required by the Federal Reserve Board; and be acceptable to the Federal Reserve Board.

Once notice is received, the financial holding company may not commence any new activities or acquire a company engaged in 4(k) activities without prior approval from the Federal Reserve Board. If the deficiencies are not corrected within 180 days of receipt of the notice, the financial holding company may be ordered to divest control of any depository institution subsidiary; alternatively, the financial holding company may, at its election, cease engaging in activities other than those permissible under section 4c(8) of the Bank Holding Company Act.[31]

What are the consequences for financial holding companies whose depository institution subsidiaries fail to maintain a satisfactory or better CRA rating?

As in the case of a failure to meet the well-capitalized and well-managed maintenance requirements, prohibitions are placed on financial holding companies whose depository institution subsidiaries fail to maintain a satisfactory or better CRA rating. Although the Federal Reserve Board will notify the financial holding company if any of its depository institutions cease to meet capital or management requirements, notice of noncompliance for depository institutions failing to

[29] See SR 00-1, February 8, 2000.
[30] See sections 102, 201, 202, and 217 of the Gramm-Leach-Bliley Act.
[31] See Section 103 of the Gramm-Leach-Bliley Act, 12 C.F.R. § 225.83, and SR 00-11.

maintain satisfactory or better CRA ratings is different. The financial holding company is deemed to have received notice of noncompliance once the appropriate federal banking agency has forwarded the examination report (showing a less than satisfactory CRA rating) to the insured depository institution or to the controlling financial holding company.

Once a financial holding company is deemed to have received notice, it may not commence any additional 4(k) activities, nor may it directly or indirectly acquire control of a company engaged in any 4(k) activities.[32]

The cure provisions required for failure to maintain well-capitalized and well-managed status do not apply to failure to maintain a satisfactory or better CRA rating.

If a financial holding company has not yet utilized its expanded powers, is it still required to meet the well-capitalized and well-managed maintenance requirements?

Yes. Once financial holding company status is achieved, the capital, management, and CRA requirements must be met regardless of whether the financial holding company has begun to engage in permissible FHC activities.

Permissible Activities

Does the Gramm-Leach-Bliley Act authorize financial holding companies to engage in commercial activities?

The Gramm-Leach-Bliley Act does not generally authorize financial holding companies to engage in commercial activities. However, it does authorize financial holding companies to engage in activities with commercial characteristics, such as complementary activities, merchant banking, and a limited amount of commercial activity by nonbanking companies that become financial holding companies.[33]

In accordance with the act, what activities may financial subsidiaries of national banks engage in?

National banks may own or control subsidiaries that engage, as principal or agent, in activities that are not permissible for national banks to engage in directly. National banks may apply to the OCC to engage in such activities through a "financial subsidiary." Financial subsidiaries of national banks may engage in all 4(k) activities, except insurance underwriting, providing or issuing annuities, real estate investment and development, and merchant banking.[34]

Can state member banks engage in activities that are authorized for financial subsidiaries?

State member banks may own or control subsidiaries that engage, as principal, in activities that are permissible for national banks to conduct through financial subsidiaries, if they comply with the conditions and limitations that apply to national banks.[35]

Can bank holding companies sell title insurance on an agency basis?

Bank holding companies are limited to activities that have been determined to be closely related to banking under section 4c(8) of the Bank Holding Company Act. Acting as an agent for the sale of title insurance is not among these activities. However, financial holding companies may engage in title insurance agency activities, pursuant to section 4(k)(4)(B) of the Bank Holding Company Act.

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[32] See Section 103 of the Gramm-Leach-Bliley Act, 12 C.F.R. § 225.83, and SR 00-11.
[33] See section103 of the Gramm-Leach-Bliley Act.
[34] See sections 121(a) and 122 of the Gramm-Leach-Bliley Act.
[35] See section 121(d) of the Gramm-Leach-Bliley Act.

What new activities has the Federal Reserve Board authorized for financial holding companies under act?

The Federal Reserve Board has ruled that acting as a "finder" is an activity that is incidental to financial activity.[36] Finders may act through any means to bring buyers and sellers of products and services together for transactions that the parties negotiate and consummate themselves. Finders may, among other things, host an internet marketplace consisting of links to the Web sites of buyers and sellers. Finders may also operate Web sites that allow buyers and sellers to post information concerning products and services and to enter into transactions among themselves.

What new activities have been proposed for financial holding companies?

The Federal Reserve Board has sought comment on whether real estate brokerage and real estate management activities are financial in nature or incidental to a financial activity.[37] In addition, the Federal Reserve Board has solicited comment on proposed rules that would allow financial holding companies to engage in certain types of data storage, internet, portal hosting, and advisory activities involving data processing as complementary activities.[38]

Notices

How must financial holding companies notify the Federal Reserve in order to engage in activities that are financial in nature?

Financial holding companies that propose to engage in an activity or that acquire control or shares of a company engaged in 4(k) activities must provide written notice to the appropriate Federal Reserve Bank within 30 calendar days of the commencement of the activities or the acquisition. The Federal Reserve Board has designated forms that domestic and foreign financial holding companies must use to satisfy the post-transaction notice requirement[39] The notice should describe the activity or identify the name of the company acquired and describe its activities.

No notice is required in connection with the acquisition of shares of a company if the financial holding company would not control the company after the acquisition.[40]

What approval is required for financial holding companies to engage in complementary activities?

Financial holding companies may engage in any nonfinancial activity that the Federal Reserve Board determines is complementary to financial activity and does not pose substantial risk to the safety and soundness of depository institutions or to the financial system. Notice is required 60 days prior to engaging in complementary activities.[41]

What is the divestiture period for impermissible commercial holdings of a nonbanking company that becomes a financial holding company?

When a nonbanking company that is predominately engaged in financial activities becomes a financial holding company, the organization has up to 10 years to divest its impermissible commercial holdings. However, the financial holding company may apply to the Federal Reserve Board to receive a five-year extension.[42]

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[36] See 65 F.R. 80735, December 22, 2000, and the correction in 66 F.R. 19081, April 13, 2001.
[37] See 66 F.R. 307, January 3, 2001, and 66 F.R. 12440, February 27, 2001.
[38] See 65 F.R. 80384, December 21, 2000.
[39] Domestic financial holding companies should use the FR Y-10, and foreign banking organizations should use the FR Y-10F. See 66 F.R. 406, n. 15, January 3, 2001.
[40] See 12 C.F.R. § 225.87; SR 00-1, February 8, 2000.
[41] See section 103(c) of the Gramm-Leach-Bliley Act and 12 C.F.R. § 225.89.
[42] See section 103 of the Gramm-Leach-Bliley Act.

How do financial holding companies request that the Board designate an activity as financial in nature or incidental to financial activity?

Financial holding companies should submit a request to the Board that identifies the activity and explains in detail why it should be considered financial in nature. The Board will consult with the Secretary of the Treasury and will endeavor to make a decision on the request within 60 days following the consultative process.[43]

[43] See section 103 of the Gramm-Leach-Bliley Act and 12 C.F.R. § 225.88

References and Resources

History of Affiliations between Banking, Securities, and Insurance Entities

Year	Event
1933	Glass-Steagall Act separates commercial and investment banking.
1956	Bank Holding Company Act limits the activities of companies with two or more bank subsidiaries to managing and controlling banks or closely related activities.
1970s	Securities firms begin offering deposit-like mutual fund accounts paying market interest rates with access to funds through drafts.
1980	Monetary Control Act begins the process of deregulating interest rates on deposit accounts, allows NOW accounts, and expands thrift powers.
1982	Garn-St. Germain Act authorizes money market deposit accounts and prohibits bank holding companies from providing insurance activities, except in specifically enumerated instances. OCC approves the formation of an operating subsidiary to engage in discount securities brokerage for the general public.
1983	Federal Reserve Board approves a bank holding company's acquisition of a discount securities broker.
1987	Supreme Court approves an OCC action allowing national banks to own discount brokerage subsidiaries. Federal Reserve Board approves bank holding company applications to underwrite and deal in certain ineligible securities at the 5 percent–10 percent level.
1989	Federal Reserve Board approves bank holding company applications to expand securities underwriting and dealing to all corporate debt and equity.
1990	Courts upholds an OCC action allowing a national bank to form an operating subsidiary to sell insurance throughout the United States from a town with a population of 5,000 or less.
1995	Supreme Court decides that national banks can sell annuities because they are investment products, not insurance.
1996	Federal Reserve Board increases the gross revenue limit on ineligible securities underwriting and dealing to 25 percent and eliminates cross-marketing restrictions. Supreme Court rules that state law cannot significantly interfere with a national bank's exercise of its authority to sell insurance from a small town.
1997	Federal Reserve Board eliminates section 20 firewalls and adopts less restrictive operating standards.
1998	Federal Reserve Board approves Travelers' application to acquire Citicorp.
1999	President Clinton signs the Gramm-Leach-Bliley Act.
2000	Federal Reserve Board approves Charles Schwab's application to acquire U.S. Trust.

Federal Reserve Board Actions

The Federal Reserve Board has taken the following actions to implement the provisions of the Gramm-Leach-Bliley Act:

Date	Action
March 11, 2000	An interim rule listing financial activities that are permissible for financial holding companies becomes effective. This interim rule, which amends Regulation Y (bank holding companies), establishes procedures for financial holding companies to engage in approved financial activities. It also establishes procedures by which parties may ask the Federal Reserve Board to approve additional activities as financial in nature or as incidental to or complementary to financial activity.
	Each federal banking agency implements the new CRA examination cycle.
	Amendments to the Electronic Funds Transfer Act become effective.
	An interim rule is approved, permitting qualifying state member banks to establish financial subsidiaries and, thereby, to engage in activities that have been designated financial in nature or incidental to financial activities. An interim rule takes effect, which applies certain section 20 operating standards to the securities affiliates of financial holding companies.
March 13, 2000	Announcement that the elections of 117 bank holding companies and foreign banking organizations to become or to be treated as financial holding companies are effective.
May 10, 2000	Federal Reserve Board, FDIC, OCC, and OTS approve final regulations for the privacy of consumer financial information.
December 4, 2000	Federal Reserve Board, FDIC, OCC, and OTS adopt consumer protection rules for insurance products sold by depository institutions.
December 13, 2000	Federal Reserve Board determines that acting as a "finder" is incidental to financial activity and, therefore, is permissible for financial holding companies. The rule provides that finders may act through any means to bring buyers and sellers of products and services together for transactions that the parties negotiate and consummate themselves.
December 21, 2000	Federal Reserve Board approves a final rule setting forth procedures for domestic bank holding companies and foreign banking organizations to qualify as financial holding companies. The final rule reflects public comments submitted on the interim rule (in effect since March 11, 2000). Banking agencies approve CRA Sunshine provisions.
	The Federal Reserve Board publishes an interim rule defining three categories of activities listed in section 4(k)(5) of the Bank Holding Company Act as financial in nature or incidental to financial activity. The interim rule also establishes a mechanism through which financial holding companies or other interested parties may request that the Board find, by order, that particular specific activities fall within one of the three categories.

January 10, 2001	Federal Reserve Board and the Secretary of the Treasury approve a joint final rule governing the merchant banking activities of financial holding companies.
January 17, 2001	Federal Reserve Board, FDIC, OCC, and OTS adopt guidelines for financial institutions to safeguard confidential customer information.
March 1, 2001	Federal Reserve Board publishes a final rule amending Regulation E (electronic funds transfers) to implement act's provisions requiring the disclosure of ATM fees.
March 14, 2001	The federal banking regulatory agencies approve a joint rule extending the effective date of consumer protection rules for the sale of insurance products by depository institutions on their premises or on their behalf. The new effective date is October 1, 2001, rather than the original effective date of April 1, 2001.
March 22, 2001	Federal Reserve Board announces procedures for filing documents required by the CRA sunshine provisions of the Federal Deposit Insurance Act.
May 4, 2001	Federal Reserve Board approves an interim final rule (under sections 23A and 23B), requiring institutions to adopt policies and procedures designed to monitor, manage, and control credit exposures arising from derivatives transactions with affiliates and intraday credit extensions to affiliates. The effective date is January 1, 2002. The Federal Reserve Board also solicits comments on a comprehensive proposed rule dealing with sections 23A and 23B.
August 16, 2001	Federal Reserve Board adopts a final rule authorizing state member banks that comply with certain requirements to control or hold an interest in financial subsidiaries, which may conduct certain financial activities that are not permissible for the parent bank to conduct directly. The effective date is September 17, 2001.

Press releases and full text for all Board actions can be found at
www.federalreserve.gov/boarddocs/press/boardacts/2001/
and
www.federalreserve.gov/boarddocs/press/boardacts/2000/

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Web Resources

Text, conference report, and summary of the provisions of the Gramm-Leach-Bliley Act
www.senate.gov/~banking/conf/

Financial holding company regulations
www.federalreserve.gov/BoardDocs/Press/BoardActs/2000/200012213/default.htm

Federal Register documents
www.access.gpo.gov/su_docs/aces/aces140.html

SR Letter 00-01, "Procedures to Become a Financial Holding Company and Guidance Regarding the Initial Monitoring of Acquisitions and the Commencement of New Activities by Financial Holding Companies"
www.federalreserve.gov/boarddocs/srletters/2000/sr0001.htm

Supervision and Regulation Letters
www.federalreserve.gov/boarddocs/srletters/

Listing of financial holding companies
www.federalreserve.gov/generalinfo/fhc/default.htm

Financial Subsidiaries of State Member Banks
www.federalreserve.gov/boarddocs/press/boardacts/2001/

Financial Subsidiaries of National Banks
http://www.occ.treas.gov/ftp/regs/2000-16a.txt

Privacy regulation
www.occ.treas.gov/ftp/regs/2000-21b.txt

Overview of issues relating to the Gramm-Leach-Bliley Act
www.phil.frb.org/src/glba.html