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[FR Doc. 96–28676 Filed 11–6–96; 8:45 am]

BILLING CODE 6732–01–M

FEDERAL RESERVE SYSTEM

[Docket No. R–0701]

Review of Restrictions on Director, Officer and Employee Interlocks, Cross-Marketing Activities, and the Purchase and Sale of Financial Assets Between a Section 20 Subsidiary and an Affiliated Bank or Thrift

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Notice.

SUMMARY: The Board is amending three of the prudential limitations established in its decisions under the Bank Holding Company Act and the Glass-Steagall Act permitting a nonbank subsidiary of a bank holding company to underwrite and deal in securities. The Board is easing or eliminating the following restrictions on these so-called section 20 subsidiaries: the prohibition on director, officer and employee interlocks between a section 20 subsidiary and its affiliated banks or thrifts (the interlocks restriction); the restriction on a bank or thrift acting as agent for, or engaging in marketing activities on behalf of, an affiliated section 20 subsidiary (the cross-marketing restriction); and the restriction on the purchase and sale of financial assets between a section 20 subsidiary and its affiliated bank or thrift (the financial assets restriction).

EFFECTIVE DATE: January 7, 1997.

FOR FURTHER INFORMATION CONTACT: Gregory Baer, Managing Senior Counsel (202) 452–3236, Thomas Corsi, Senior Attorney (202) 452–3275, Legal Division; Michael J. Schoenfeld, Senior Securities Regulation Analyst (202) 452–2781, Division of Banking Supervision and Regulation; for the hearing impaired only, Telecommunications Device for the Deaf (TDD), Dorothea Thompson (202) 452–3544.

SUPPLEMENTARY INFORMATION:

I. Background

In its section 20 orders, the Board has established a series of firewalls designed to prevent securities underwriting and dealing risk from being passed from a section 20 subsidiary to an affiliated insured depository institution, and to prevent the federal safety net from being extended to subsidize this activity.[1] The firewalls also reduce the potential for conflicts of interest, unfair competition, and other adverse effects that may arise from securities underwriting and dealing. In adopting these restrictions, the Board stated that it would continue to review their appropriateness in the light of its experience supervising section 20 subsidiaries.

The Board originally sought comment on changes to the interlocks, cross-marketing and financial assets restrictions on July 10, 1990. The Board received forty responses to its notice, with comments coming from banks, securities firms, trade associations and other members of the public. However, because legislation affecting the section 20 firewalls was introduced shortly after the Board sought comment, and has been introduced intermittently in the years since, the Board deferred further action.[2]

On July 31, 1996, the Board announced that it was reopening the three firewalls for comment, and broadening the changes proposed. An additional 41 public comments were received. Commenters included 20 bank holding companies, eight bank trade associations, seven foreign banks, one securities trade association, and four members of the public.

Commenters expressed strong support for the three proposed amendments. Of 41 public commenters, only four opposed one or more of the proposals. Many commenters suggested that they be expanded. Commenters stated that adoption of the Board's proposals was vital to the ability of section 20 subsidiaries to compete with other providers of financial services and to provide bank holding company customers with the array of financial products and services they require. Commenters stressed that the firewalls were not required by the Glass-Steagall Act and imposed substantial costs that could not be justified by any corresponding benefit.

Three commenters made general objections to this proposal and those concerning the section 20 revenue test. A securities trade association urged the Board to defer action indefinitely in order to allow Congress to undertake comprehensive reform of the financial services system. An individual commenter argued that recent examples of malfeasance in the securities markets argued against allowing bank holding companies to expand their securities activities. Another individual argued that any action that allows bank holding companies to engage in more investment banking creates an opportunity for huge losses, and that re-regulation rather than deregulation is in order.

II. Final Order

After considering the comments, the Board has decided to repeal the cross-marketing restriction as proposed, and amend the interlocks and financial assets restrictions in ways similar to those proposed. The Board has concluded that with these amendments, limited underwriting and dealing in securities would remain closely related to banking and a proper incident thereto, and thus permissible under section 4(c)(8) of the Bank Holding Company Act, because substantial benefits to efficiency, convenience and competition from these amendments outweigh any minimal costs.

As detailed below, the Board's experience administering these firewalls indicates that the existing restrictions are more restrictive than necessary to serve their intended purposes. Furthermore, their repeal or constriction

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[1] *See, e.g., J.P. Morgan & Co., The Chase Manhattan Corp., Bankers Trust New York Corp., Citicorp, and Security Pacific Corp.*, 75 Federal Reserve Bulletin 192, 202–03 (1989) (hereafter, *1989 Order*); *Citicorp, J.P. Morgan & Co., and Bankers Trust New York Corp.*, 73 Federal Reserve Bulletin 473, 492 (1987) (hereafter, *1987 Order*).

The interlocks and cross-marketing restrictions were included in the Board's *1987 Order* authorizing certain section 20 subsidiaries to underwrite and deal in four limited types of debt securities, and were repeated in the Board's *1989 Order* authorizing certain section 20 subsidiaries to underwrite and deal in all types of debt and equity securities. *See 1987 Order* at 503, 504 (Firewalls #10 and #13); *1989 Order* at 215 (Firewalls #13 and #16). The financial assets restriction was included in the 1989 Order but not the 1987 Order. *See 1989 Order* at 216 (Firewall #22). All three have since been applied to foreign banks operating section 20 subsidiaries. *Canadian Imperial Bank of Commerce, The Royal Bank of Canada, Barclays PLC and Barclays Bank PLC*, 76 Federal Reserve Bulletin 158, 172 (1990) (hereafter, *1990 Order*) (Firewalls #13, #16, and #22).

[2] These older comments, many of which have been superseded by a subsequent comment or mooted by changes to the amendments proposed, are not discussed in detail below but were considered by the Board.

should lower operating costs for existing section 20 subsidiaries and eliminate significant barriers to entry for smaller bank holding companies considering the establishment of a section 20 subsidiary. The amendments should also benefit customers. Bank holding companies will be able to serve their customers needs more effectively and should be able to pass along cost savings derived from improved efficiency; new entrants should provide better service for small and mid-size issuers, and increased competition may lower costs.

A. Interlocks Restriction

1. Background

The interlocks restriction currently prohibits all director, officer and employee interlocks between a section 20 subsidiary and an affiliated bank.[3] The restriction seeks to ensure that the risks of underwriting and dealing are not passed from a section 20 subsidiary to an affiliated bank.[4]

The Board proposed to eliminate the firewall entirely or replace it with a more narrow restriction. With respect to directors, the Board sought comment on whether to prohibit a majority of the board of directors of a section 20 subsidiary from being composed of directors, officers or employees of an affiliated bank, and a majority of the board of directors of a bank from being composed of directors, officers or employees of an affiliated section 20 subsidiary. The Board also sought comment on whether it should limit the prohibition on officer interlocks to only the chief executive officer or senior executive officers of each company.

2. Summary of Comments

Commenters devoted the majority of their comments to this restriction, stressing that its elimination would increase the operational efficiency of bank holding companies and allow entry by smaller organizations that otherwise could not bear the costs of staffing a section 20 subsidiary. Commenters also stated that there was no need for an interlocks restriction to prevent risk from being passed from a section 20 subsidiary to an affiliated bank.

More specifically, commenters stated that the existing interlocks restriction causes redundant staffing and operational inefficiencies by precluding functional reporting, supervision and coordination between complementary section 20 and bank business units. For example, one large bank holding company commenter noted that if the restriction were eliminated, senior personnel who oversee the treasury function in a bank could oversee the related businesses in an affiliated section 20 subsidiary; similarly, a senior officer serving as the global head of a particular business, such as Fixed Income or Emerging Markets, could participate in the management of each of the entities involved in those businesses. Another large bank holding company commenter explained that it had been forced to move its project finance business out of its section 20 subsidiary because of the interlocks restriction; instead, the company has placed virtually all offshore employees, including project finance employees, in its lead bank or its subsidiaries.

Many commenters stressed that by preventing a centralized management structure, the interlocks restriction makes it more difficult for bank holding companies to control and manage risk. Indeed, commenters argued that restricting interlocks may actually increase risks to the bank holding company by preventing the most experienced and responsible members of the organization from monitoring risk.

Commenters also noted that the Glass-Steagall Act does not require an interlocks restriction, and that the Board has not restricted interlocks between a bank and any type of affiliate other than a section 20 subsidiary. Commenters stated that customer confusion and challenges to corporate separateness have not arisen with respect to these other affiliates. Commenters also argued that, with respect to section 20 subsidiaries, any such concerns are adequately addressed by other restrictions.

Commenters stated that SEC and Federal Reserve capitalization requirements for section 20 companies and the restrictions on inter-affiliate transactions contained in sections 23A and 23B of the Federal Reserve Act would be sufficient to ensure that the companies are operated independently, and that disclosures would be sufficient to prevent customer confusion.

Commenters generally opposed the Board's proposed alternatives to eliminating the restriction. The suggested restriction on officer interlocks was more frequently and deeply criticized, with commenters arguing that interlocks at the senior level were most necessary for effective management. Although commenters also generally opposed any restriction on director interlocks, a few commenters noted that it was neither as great an impediment to sound management nor as great a compliance burden as the restriction on officer interlocks.

3. Final Order

The Board is adopting the amendments substantially as proposed, and thereby substantially reducing the scope of the interlocks restriction. The Board has concluded that a blanket prohibition on director, officer and employee interlocks is an unnecessary restraint under section 4(c)(8) of the Bank Holding Company Act. Nonetheless, for the reasons set forth below, the Board has concluded that a narrow interlocks restrictions would further ensure corporate separateness at minimal cost. Accordingly, the Board is prohibiting directors, officers or employees of a bank from serving as a majority of the board of directors or the chief executive officer of an affiliated section 20 subsidiary, and prohibiting directors, officers or employees of a section 20 subsidiary from serving as a majority of the board of directors or the chief executive officer of an affiliated bank. The Board is imposing no restriction on employee interlocks. The Board intends to review these restrictions after these changes to the firewalls, and any subsequent changes made after a more comprehensive review, have been implemented.

a. *Officer and director interlocks/ Corporate separateness.* Courts generally prefer to honor the corporate form and recognize corporations as legal entities separate from their shareholders. ''Piercing the corporate veil'' refers to the judicially imposed exception to this principle by which courts disregard corporate separateness and impose liability on an individual or corporate shareholder or corporate sibling. In deciding whether one company should be held liable for the liabilities of another, courts generally require 1. that the corporate form be used to commit a fraud or injustice on the plaintiff; and 2. that one company so dominate another that they should be considered, and held liable, as one.[5]

[3] Hereafter, references to banks include thrifts.

[4] In specific cases, the Board has authorized limited officer or director interlocks between a section 20 subsidiary and its affiliated banks. *See, e.g., National City Corporation,* 80 Federal Reserve Bulletin 346, 348–9; *Synovus Financial Corp.,* 77 Federal Reserve Bulletin 954, 955–56 (1991); *Banc One Corporation,* 76 Federal Reserve Bulletin 756, 758 (1990).

[5] In making the latter determination, courts consider a multitude of factors. These factors include: (1) the absence of the formalities that are part and parcel of corporate existence; (2) inadequate capitalization; (3) overlap in ownership, officers, directors, and personnel; (4) common office space, address and telephone numbers of corporate entities; (5) the amount of business discretion displayed by the allegedly dominated corporation; (7) whether the dominated corporation is dealt with at arms length; (8) whether the corporations are

Repeal of the interlocks and cross marketing restrictions would allow increased synergies in the operation of a section 20 subsidiary and its bank affiliates. Persons may be employed by both companies, and the trend toward common management of like business functions could accelerate, with reporting lines running between companies. While such coordinated management and commonality of personnel generally are not sufficient to justify disregarding the corporate form, they are sometimes combined with other factors to justify such a decision.

On the other hand, SEC rules and other Board firewalls require that a section 20 subsidiary be adequately capitalized, and the examination process ensures that the corporate formalities are maintained and that holding company affiliates deal with each other on arm's-length terms, as required by section 23B of the Federal Reserve Act.[6] These are important factors considered by courts in deciding whether to pierce the corporate veil.

After weighing these considerations, the Board has concluded that a restriction on interlocks at the most senior level might provide some further assurance of corporate separateness. The director interlocks restriction should clarify that the goals of the section 20 subsidiary, while they may be intertwined with an affiliated bank, are independent of the bank. The chief executive officer interlocks restriction should clarify that control of the day-to-day activities of each company is independent of the other.

Of equal note, these minimal restrictions should not impose significant costs to the bank holding company. Finding qualified directors who are not connected to an affiliate (and who could be drawn from the holding company) should not burden a section 20 subsidiary or a bank. Prohibiting a section 20 subsidiary or a bank from designating a director, officer or employee of an affiliate as its chief executive officer is a minimal burden, as the job of chief executive officer should be a full-time occupation.

b. *Employee interlocks/Vicarious liability.* While employee interlocks could be considered in a decision about whether to pierce the corporate veil, the employee interlocks restriction serves primarily to prevent customer confusion about the identity of the customer's counterparty, and potential vicarious liability of the bank for the actions of an affiliated section 20 subsidiary. Thus, the employee interlocks restriction is more closely related to the cross-marketing restriction, which has the same aim.

A bank could be held vicariously liable for the actions of an affiliate's employee if a customer reasonably believed that the employee were acting under the actual or apparent authority of the bank. Clearly, if a section 20 employee were also an employee of the bank (as elimination of the employee interlocks restriction would allow) and was also selling bank products (as elimination of the cross-marketing restriction would allow), the potential for such liability might increase.

However, for the reasons discussed below in connection with the cross-marketing restriction, the Board has concluded that current disclosure requirements and practices should be sufficient insurance against vicarious liability. The Board emphasizes that supervision by federal and state banking agencies will need to continue with increased vigilance in order to ensure that the disclosures are adequate and are provided whenever appropriate.

4. Continued Supervisory Concerns

Although the Board has concluded that a broad interlocks restriction is unnecessary to ensure corporate separateness or prevent customer confusion, proper risk management may require further restriction of interlocks on a case-by-case basis. For example, an employee responsible for custodial services at a bank generally should not be involved in trading at an affiliated section 20 subsidiary. In such cases, the problem is not with the dual employment *per se*, but rather with the potential for conflicts of interest or other risks arising from the nature of the employee's duties (be they conducted at the bank or the section 20 subsidiary). These matters will continue to be addressed in the supervisory process by ensuring prudent internal controls—for example, proper segregation of duties—to manage conflicts of interest and prevent violations of law.

B. Cross-marketing Restriction

1. Background

The Board's section 20 orders prohibit a bank from acting as agent for, or engaging in marketing activities on behalf of, an affiliated section 20 subsidiary.[7] This restriction was intended to prevent customers from being confused about the identity of their counterparty, and perhaps attempting to hold the bank liable for actions of an affiliated section 20 subsidiary. Such liability could arise under a variety of legal theories, most notably vicarious liability (or *respondeat superior*), where a company can be liable for the actions of its agent, regardless of whether the company itself was at fault.[8] The Board sought comment on whether to eliminate this restriction.

2. Summary of Comments

Commenters stated that the existing restriction prevents bank holding companies from serving their customers effectively. One commenter explained that if a customer wishes to purchase a security from a section 20 subsidiary and also enter into a related contract with a bank affiliate for the purposes of managing the risks of that security, the cross-marketing restriction requires the customer to deal and communicate separately with bank and section 20 company representatives. Another commenter explained that the restriction complicates the client calling efforts of its relationship managers. The commenter found this restriction particularly unjustifiable in the wholesale market, where section 20 subsidiaries do the majority of their business and where the role of each company is well understood. Finally,

treated as independent profit centers; (9) the payment or guarantee of debts of the dominated corporation by other corporations in the group; and (10) whether the corporation in question has property that was used by other of the corporations as if it were its own. *See, e.g., W. Passalacqua Builders v. Resnick Developers,* 933 F.2d 131 (2d Cir. 1991) (applying New York common law).

[6] 12 U.S.C. 371c-1.

[7] The Board has allowed a few limited exceptions to the cross-marketing restriction. *See Letter Interpreting Section 20 Orders,* 81 Federal Reserve Bulletin 198 (1995).

[8] One of the commenters to the 1990 notice cautioned that liability could arise not only under the legal theory of vicarious liability but also under secondary liability as a controlling person under Section 20(a) of the Securities Exchange Act of 1934, aiding and abetting, and conspiracy.

To be liable under the Securities Exchange Act for the actions of an employee, a bank would have to control the actions of the employee at the section 20 subsidiary. However, the Act specifically provides that no liability can be imposed if the controlling person can show that it acted in good faith and did not directly or indirectly induce the act or acts constituting the violation, *see* 15 U.S.C. § 78(t)(a), and courts have held that a bank may demonstrate its good faith under section 20(a) through maintenance and enforcement of ''a reasonable and proper system of supervision and internal control.'' *See Hollinger v. Titan Capital Corp.,* 914 F.2d 1564, 1576 (9th Cir. 1990).

In order to be liable for vicarious liability based on civil conspiracy, a defendant must have knowingly and substantially assisted in the fraud. Aiding and abetting liability, which in 1990 required a showing akin to civil conspiracy, was eliminated as a private cause of action in *Central Bank v. First Interstate Bank,* 511 U.S. 164 (1994). The SEC may still bring an action for civil money penalties for aiding and abetting, with penalties determined by statute. *See* 15 U.S.C. 78u(d)(1), (d)(3).

another commenter noted that its customers had frequently expressed frustration with the multiplicity of contacts and communications required by the current firewall.

Commenters stated that repeal would eliminate these inefficiencies. One commenter explained that repeal would enable a single officer—whether in a bank or a section 20 subsidiary—to market the full range of products offered by the holding company group, and better tailor the group's products to the needs of the customer. Bank holding company commenters also stated that repeal of the cross-marketing restriction would eliminate a competitive inequality between them and their investment banking competitors, who market their products without restrictions. One commenter noted that investment banks have expanded beyond traditional financial advisory and securities underwriting services into bank loan syndications, bridge financings and private equity investment.

Commenters also stated that existing disclosure requirements—most notably the Interagency Statement on Retail Sales of Nondeposit Products—were sufficient to address any concerns about customer confusion. One commenter observed that clients for sophisticated financial products are unlikely to be confused about the structure of a proposed transaction or the corporate identity of the counterparties involved, and that where the insured status of a counterparty may have significance, such disclosure requirements are sufficient to ensure that the necessary information is available to the customer.

Three commenters raised specific objections to repeal of the cross-marketing firewall. A securities trade association stated that while it was aware that safety and soundness and investor protection concerns were the paramount issues causing the Board to impose the various firewalls, the cross-marketing restriction has at least partially maintained a level of competitive fairness between section 20 subsidiaries and other securities firms by limiting a section 20 subsidiary's ability to market its products and services through an affiliated bank's retail branch system—an opportunity not available to other securities firms. A bank trade association urged the Board to allow cross-marketing only on a case-by-case basis in order to avoid the danger that products or services could be packaged in a way that would give bank holding companies an unfair competitive advantage. Another commenter stated that repeal of the cross-marketing restriction would pose risks to the public, citing a study showing that some consumers mistakenly believe that money market mutual funds are insured.

3. Final Order

The Board has decided to repeal the cross-marketing restriction. As noted by the commenters, existing disclosure requirements adequately address concerns about customer confusion. The Interagency Statement on Retail Sales of Nondeposit Products states that, for any sale of a non-deposit product by a bank employee or on bank premises, the customer must receive and acknowledge a written statement that the product being sold is not federally insured, is not a deposit or other obligation of the bank and is not guaranteed by the bank, and is subject to investment risks including loss of principal.[9] Although the Interagency Statement does not apply to sales to institutional customers, the Board understands that, while obtaining acknowledgements may be infeasible, disclosures are sometimes provided. The Board believes that this is good practice, particularly in the case of individual investors. *See* 12 CFR 225.2(g)(3).

Furthermore, other firewalls require a section 20 subsidiary to provide each of its customers with a special disclosure statement describing the difference between the underwriting subsidiary and its bank affiliates, and stating that securities sold, offered or recommended by the section 20 subsidiary are not deposits, not federally insured, not guaranteed by an affiliated bank, and not otherwise an obligation or responsibility of such bank.[10] Although the disclosure firewall does not require that a section 20 subsidiary obtain an acknowledgement, the Interagency Statement would require an acknowledgement if the sale were on bank premises, and the Board understands that section 20 subsidiaries generally obtain an acknowledgement even when operating off bank premises. The Board believes that this represents good practice. Once again, supervisory efforts by the Board and other agencies will need to be emphasized in this area.

Finally, the Board notes that no serious problems of *respondeat superior* liability have arisen with subsidiaries engaged in underwriting eligible securities, despite the absence of a cross-marketing firewall.

The concerns raised by commenters do not argue for retaining the cross-marketing restriction. First, although banks could in theory package their products in order to gain an unfair competitive advantage, this danger is addressed specifically by the antitrust laws, most notably the Sherman Act, and by a special anti-tying restriction contained in section 106 of the Bank Holding Company Act Amendments of 1970. 12 U.S.C. 1972(1). Second, even assuming that the cross-marketing firewall helps to create competitive equality between section 20 subsidiaries and other securities firms, as one commenter stated, the Board does not believe that keeping customers ignorant of business opportunities is an effective or appropriate way to maintain competitive equality.

4. Continued Compliance Concerns

Furthermore, member banks should be aware that repeal of the cross-marketing firewall does not relieve them of their obligation to comply with sections 16 and 21 of the Glass-Steagall Act. 12 U.S.C. 24 (Seventh); 12 U.S.C. 378a. Although the Board will no longer impose a blanket prohibition on a member bank's acting as agent for an affiliated section 20 subsidiary, the bank will still be prohibited from distributing securities underwritten by the section 20 subsidiary.

C. Restriction on Purchase and Sale of Financial Assets

1. Background

The Board sought comment on amending the financial assets restriction, which generally prohibits a bank from purchasing financial assets from, or selling such assets to, an affiliated section 20 subsidiary. An existing exception to this restriction allows the purchase or sale of U.S. Treasury securities or direct obligations of the Canadian federal government at market terms, provided that they are not subject to repurchase or reverse repurchase agreements between the underwriting subsidiary and its bank affiliates. The Board sought comment on whether it should expand this exception to include the purchase or sale of any assets with a sufficiently broad and liquid market to ensure that the transaction is on market terms.

2. Summary of Comments

Commenters strongly favored an expanded exception to the restriction on the purchase and sale of financial assets, though many commenters favored eliminating the restriction altogether. Several commenters argued that the financial assets restriction was unduly broad to the extent it prohibits a bank from purchasing and selling securities

[9] Compliance with the Interagency Statement is examined for by the federal banking agencies.

[10] *E.g. 1989 Order* at 215.

that it is permitted by statute to purchase and sell for its own account. Commenters noted that sections 16 and 21 of the Glass-Steagall Act, and regulations adopted pursuant thereto, require that a bank determine that ''there is adequate evidence that the obligor will be able to perform all that it undertakes to perform in connection with the security, including all debt service requirements, and that the security is marketable'' before purchasing a security.[11] Commenters contended that these restrictions fully address the issues of credit quality and liquidity in bank investments.

Another commenter stressed that regional bank holding companies have legitimate reasons for asset transactions between a section 20 company and its affiliated bank. Because the securities distribution side of regional section 20 companies tends to be dominated by individual investors and smaller institutional and corporate investors, a bank holding company might find it economically advantageous for its section 20 subsidiary to acquire securities which can both be sold to the bank for its investment portfolio and distributed by the section 20 subsidiary to its investor clients. The commenter stated that such commingled transactions enable the institution to obtain securities in the open market at more favorable terms than would otherwise be available at lower volume.

A securities trade association objected to the proposal on the grounds that it would permit banks to sell financial assets to, or purchase such assets from, affiliated section 20 subsidiaries on terms or under conditions that would not be available to other securities firms, in effect subsidizing the activities of their affiliated section 20 subsidiaries. The commenter also expressed concern that banks could provide their section 20 affiliates with access to certain financial assets either earlier, or in greater amounts, than other securities firms.

3. Final Order

The Board is expanding the exception to the financial assets restriction, but using a more definite standard than that proposed. Rather than allowing the purchase or sale of any security with a ''broad and liquid market,'' the Board is extending the exception to ''assets having a readily identifiable and publicly available market quotation and purchased at that market quotation.'' Asset purchases meeting this price availability standard are already exempt from the quantitative and qualitative restrictions on inter-affiliated funding contained in sections 23A and 23B of the Federal Reserve Act. 12 U.S.C. 371c(d)(6); 12 U.S.C. 371c–1(d)(3). Use of the same standard is appropriate here. First, the same policy is being served: ensuring that an inter-affiliate transaction is so verifiably arm's-length so as not to require federal regulation of its terms. Second, use of the same standard will ease compliance burden for banks, who are experienced in administering it. Indeed, for any purchase of assets by a bank from an affiliated section 20 subsidiary, the bank will already be required to ensure compliance with this standard for purposes of sections 23A and 23B. Third, compliance with this standard would ensure that section 20 affiliates would not gain a competitive advantage over other securities firms through asset sales to their affiliated banks.

The Board has decided to retain for now the financial assets restriction to the extent that it prohibits a purchase or sale of less liquid assets and any purchase or sale of assets subject to a repurchase or reverse repurchase agreement. Any further changes to the financial assets restriction will be considered in conjunction with other funding firewalls, as part of a more comprehensive review of all the remaining firewalls between a section 20 subsidiary and its affiliated banks.

Revised Amendment to Firewalls

The Board is amending the section 20 firewalls as follows:

Interlocks Restriction

1987 and 1989 Orders (Domestic Bank Holding Companies)

Directors, officers or employees of a bank or thrift shall not serve as a majority of the board of directors or the chief executive officer of an affiliated section 20 subsidiary, and directors, officers or employees of a section 20 subsidiary shall not serve as a majority of the board of directors or the chief executive officer of an affiliated bank or thrift. The underwriting subsidiary will have separate offices from any affiliated bank or thrift.[***]

1990 Order (Foreign Banks)

Directors, officers or employees of Applicant's U.S. bank or thrift subsidiaries, branches or agencies shall not serve as a majority of the board of directors or the chief executive officer of an affiliated section 20 subsidiary, and directors, officers or employees of a section 20 subsidiary shall not serve as a majority of the board of directors or the chief executive officer [+ + +] of an affiliated U.S. bank or thrift subsidiary, branch or agency of Applicant, except that the manager of a branch or agency may act as a director of the underwriting subsidiary. The underwriting subsidiary will have separate offices from any bank or thrift subsidiary or branch or agency of Applicant.[###]

Cross-Marketing Restriction

1987, 1989 and 1990 Orders

The cross-marketing restriction is removed.

Financial Assets Restriction

1989 and 1990 Orders

No bank or thrift (or U.S. branch or agency of a foreign bank) shall, directly or indirectly, for its own account, purchase financial assets of an affiliated underwriting subsidiary or a subsidiary thereof or sell such assets to the underwriting subsidiary or subsidiary thereof. This limitation shall not apply to the purchase and sale of assets having a readily identifiable and publicly available market quotation and purchased at that market quotation for purposes of section 23A of the Federal Reserve Act, 12 U.S.C. 371c(d)(6), provided that those assets are not subject to a repurchase or reverse repurchase agreement between the underwriting subsidiary and its bank or thrift affiliate.

By order of the Board of Governors of the Federal Reserve System, November 1, 1996.

William W. Wiles,

Secretary of the Board.

[FR Doc. 96–28619 Filed 11–6–96; 8:45 am]

BILLING CODE 6210–01–P

Formations of, Acquisitions by, and Mergers of Bank Holding Companies

The companies listed in this notice have applied to the Board for approval, pursuant to the Bank Holding Company Act of 1956 (12 U.S.C. 1841 *et seq.*) (BHC Act), Regulation Y (12 CFR Part 225), and all other applicable statutes and regulations to become a bank

[11] 12 CFR 1.5(a).

[***] An underwriting subsidiary may have offices in the same building as a bank or thrift affiliate if the underwriting subsidiary's offices are clearly distinguished from those of the bank or thrift affiliate.

[+ + +] For purposes of this firewall, the manager of a U.S. branch or agency of a foreign bank normally will be considered to be the chief executive officer of the branch or agency.

[###] An underwriting subsidiary may have offices in the same building as a bank or thrift subsidiary or branch or agency of Applicant if the underwriting subsidiary's offices are clearly distinguished from those of the bank, thrift, branch or agency.