

# Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

## FEDERAL RESERVE SYSTEM

### 12 CFR Part 225

[Regulation Y; Docket No. R-1091]

#### Bank Holding Companies and Change in Bank Control

## DEPARTMENT OF THE TREASURY

### Office of the Under Secretary for Domestic Finance

### 12 CFR Part 1501

RIN 1505-AA84

#### Financial Subsidiaries

**AGENCIES:** Board of Governors of the Federal Reserve System and Department of the Treasury.

**ACTION:** Joint proposed rule with request for public comments.

**SUMMARY:** The Board of Governors of the Federal Reserve System and the Secretary of the Treasury jointly propose to seek comment on whether to determine by rule that real estate brokerage is an activity that is financial in nature or incidental to a financial activity and therefore permissible for financial holding companies and financial subsidiaries of national banks. The Board and the Secretary also jointly propose to solicit comment on whether real estate management activities could be considered financial in nature or incidental to a financial activity. The Board's proposed rule would amend subpart I of the Board's Regulation Y to add real estate brokerage and real estate management to the list of activities permissible for financial holding companies. The Secretary's proposed rule would amend its financial subsidiary regulations to add real estate brokerage and real estate management to the activities permissible for financial subsidiaries of national banks. The Board and the Secretary solicit comment on all aspects of the proposal.

**DATES:** Comments must be received by March 2, 2001.

**ADDRESSES:** Comments should refer to docket number R-1091 and should be mailed to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551 (or mailed electronically to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov)) and to Real Estate Brokerage and Management Regulation, Office of Financial Institution Policy, U.S. Department of the Treasury, 1500 Pennsylvania Avenue, NW., Room SC 37, Washington, DC 20220 (or mailed electronically to [financial.institutions@do.treas.gov](mailto:financial.institutions@do.treas.gov)). Comments addressed to Ms. Johnson also may be delivered to the Board's mailroom between 8:45 a.m. and 5:15 p.m. and, outside those hours, to the Board's security control room. Both the mailroom and the security control room are accessible from the Eccles Building courtyard entrance, located on 20th Street between Constitution Avenue and C Street, N.W. Members of the public may inspect comments in room MP-500 of the Martin Building between 9 a.m. and 5 p.m. on weekdays. Comments addressed to the Treasury Department may also be delivered to the Treasury Department mail room between the hours of 8:45 a.m. and 5:15 p.m. at the 15th Street entrance to the Treasury Building.

#### FOR FURTHER INFORMATION CONTACT:

*Board of Governors:* Scott G. Alvarez, Associate General Counsel (202/452-3583), or Mark E. Van Der Weide, Counsel (202/452-2263), Legal Division; Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551. For users of Telecommunications Device for the Deaf ("TDD") only, contact Janice Simms at 202/872-4984.

*Department of the Treasury:* Gerry Hughes, Senior Financial Analyst (202/622-2740); Roberta K. McInerney, Assistant General Counsel (Banking and Finance) (202/622-0480); or Gary W. Sutton, Senior Banking Counsel (202/622-0480).

#### SUPPLEMENTARY INFORMATION:

##### Background

The Gramm-Leach-Bliley Act (Pub. L. 106-102, 113 Stat. 1338 (1999)) ("GLB Act") amended the Bank Holding Company Act (12 U.S.C. 1841 *et seq.*) ("BHC Act") to allow a bank holding

company or foreign bank that qualifies as a financial holding company ("FHC") to engage in a broad range of activities that are defined by the GLB Act to be financial in nature. The GLB Act also permits FHCs to engage in other activities that the Board determines, by regulation or order and in consultation with the Secretary of the Treasury ("Secretary"), to be financial in nature or incidental to a financial activity.

The GLB Act also amended the National Bank Act (12 U.S.C. 1 *et seq.*) to allow a national bank to invest in financial subsidiaries. Financial subsidiaries may engage, with certain exceptions, in the same broad range of activities that are defined by the GLB Act to be financial in nature and, therefore, permissible for FHCs.<sup>1</sup> In addition, the GLB Act permits financial subsidiaries to engage in other activities that the Secretary determines, in consultation with the Board, to be financial in nature or incidental to a financial activity.

The American Bankers Association ("ABA") and Fremont National Bank & Trust Company, Fremont, Nebraska, have asked the Board and the Secretary (collectively, the "Agencies") to determine that real estate brokerage and management activities are financial in nature. Two additional trade associations, the Financial Services Roundtable and the New York Clearing House Association, have requested that the Board permit FHCs to engage in real estate brokerage activities.<sup>2</sup> The National Association of Realtors ("NAR") has urged the Agencies not to determine that real estate brokerage activities are financial in nature or incidental to a financial activity.

The GLB Act directs the Board to consider a variety of factors when considering a request for a determination that an activity is financial in nature or incidental to a financial activity, including (i) the purposes of the BHC Act and the GLB

<sup>1</sup> The exceptions are engaging as principal in certain insurance underwriting activities, real estate investment and development (unless otherwise expressly authorized by law), and merchant banking activities permitted in 12 U.S.C. 1843(k)(4)(H) or (I). 12 U.S.C. 24a(a)(2)(B).

<sup>2</sup> The New York Clearing House Association submitted its request on behalf of The Bank of New York Company, Inc.; Chase Manhattan Corporation; Citigroup, Inc.; J.P. Morgan, Inc.; Bankers Trust Company; Fleet Boston, Inc.; HSBC; Bank One Corporation; First Union Corporation; and Wells Fargo & Company.

Act; (ii) the changes or reasonably expected changes in the marketplace in which FHCs compete; (iii) the changes or reasonably expected changes in the technology for delivering financial services; and (iv) whether the proposed activity is necessary or appropriate to allow a FHC to compete effectively with any company seeking to provide financial services in the United States, efficiently deliver financial information and services through the use of technological means, or offer customers any available or emerging technological means for using financial services or for the document imaging of data.<sup>3</sup> The Secretary must consider a virtually identical set of factors in determining whether an activity is permissible for financial subsidiaries.<sup>4</sup> The Agencies also may consider other factors and information that they consider relevant to their determination.

The Agencies believe that the GLB Act's "financial in nature or incidental" standard represents a significant expansion of the "closely related to banking" standard that the Board previously applied in determining the permissibility of activities for bank holding companies.<sup>5</sup> In considering whether an activity was closely related to banking, the Board and the courts looked to whether banks generally (i) conduct the proposed activity, (ii) provide services that are operationally or functionally so similar to the proposed services as to equip them particularly well to provide the proposed services, or (iii) provide services that are so integrally related to the proposed services as to require their provision in a specialized form.<sup>6</sup> Because the new "financial in nature or incidental" test appears to be substantially broader than the old "closely related to banking" test, the Agencies believe that they should consider an activity to be financial in nature or incidental to a financial activity to the extent that it meets the old standard.

After considering the factors listed above and other relevant information, the Agencies propose to seek public comment on whether to adopt rules that would define real estate brokerage and real estate management as activities that

are financial in nature or incidental to a financial activity. The Board's proposed rule would amend § 225.86 of the Board's Regulation Y to add these two new activities to the list of activities permissible for FHCs. Bank holding companies and foreign banks that qualify as FHCs would be permitted to engage in real estate brokerage and real estate management by using the post-consummation notice procedure described in § 225.87 of Regulation Y. Bank holding companies and foreign banks that do not qualify as FHCs may engage only in those nonbanking activities that were permissible for bank holding companies prior to the enactment of the GLB Act and, thus, could not provide real estate brokerage or management services under the proposed rule. The Secretary's proposed rule would amend its regulations regarding financial subsidiaries to add real estate brokerage and real estate management to the activities permissible for financial subsidiaries. Qualifying national banks would be permitted to engage in these activities through financial subsidiaries by providing the Office of the Comptroller of the Currency ("OCC") with a notice under the OCC's rules.

The GLB Act requires that the Board and the Secretary consult with each other concerning any request, proposal, or application for a determination that an activity is financial in nature or incidental to a financial activity. The Agencies have consulted with each other concerning the proposed rules, and each Agency supports the other's determination to seek public comment on the proposed rules.<sup>7</sup>

## Proposed Rules

### A. Real Estate Brokerage

Real estate brokerage is the business of bringing together parties interested in consummating a real estate purchase, sale, exchange, lease, or rental transaction and negotiating on behalf of such parties a contract relating to the transaction. The activity of real estate brokerage would include acting as agent for a party to a real estate transaction; listing and advertising real estate; locating buyers, sellers, lessors, and lessees interested in engaging in real estate transactions among themselves; conveying information between the parties to a potential real estate transaction; providing advice in

connection with a real estate transaction; negotiating price and other terms on behalf of parties to a real estate transaction; and administering the closing to a real estate transaction. Real estate brokerage generally does not involve purchasing or selling real estate as principal. The business of real estate brokerage may only be conducted pursuant to state licensing laws and regulations.

As noted, prior to the passage of the GLB Act, bank holding companies were permitted to engage only in activities that the Board determined were closely related to banking under section 4(c)(8) of the BHC Act. In 1972, the Board determined that real estate brokerage was not closely related to banking for purposes of the BHC Act.<sup>8</sup> Although the GLB Act does not explicitly authorize FHCs to act as real estate brokers, the statute permits FHCs to engage in any activity that the Board, in consultation with the Secretary, has determined to be financial in nature or incidental to a financial activity. As noted, the GLB Act's "financial in nature or incidental" test is broader than the former "closely related to banking" test.

Similarly, the OCC has not permitted national banks to engage in general real estate brokerage.<sup>9</sup> Although the GLB Act does not explicitly authorize financial subsidiaries to act as real estate brokers, the statute permits financial subsidiaries to engage in any activity that the Secretary, in consultation with the Board, has determined to be financial in nature or incidental to a financial activity. For the reasons discussed below, the Agencies believe that they should seek public comment on whether real estate brokerage activities are financial in nature or incidental to a financial activity within the meaning of section 4(k)(1)(A) of the BHC Act and section 5136(a)(2)(A)(i) of the Revised Statutes.

#### 1. General "Financial in Nature or Incidental" Analysis

Some depository institutions already engage in real estate brokerage. Although, as noted, the OCC has not permitted national banks to provide

<sup>8</sup> 12 CFR 225.126(c); *Boatmen's Bancshares, Inc.*, 58 Federal Reserve Bulletin 427, 428 (1972). In 1987, as part of a proposal to authorize bank holding companies to engage in real estate investment (the "1987 Proposal"), the Board proposed permitting a bank holding company to provide real estate brokerage services in connection with real estate in which the bank holding company had an interest. See 52 FR 543 (Nov. 4, 1987); see also 50 FR 4519 (Jan. 31, 1985). The Board never adopted this proposed rule in final form.

<sup>9</sup> See OCC Interpretive Letter No. 84, reprinted in [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,159 (Apr. 3, 1979).

<sup>3</sup> See 12 U.S.C. 1843(k)(3).

<sup>4</sup> See 12 U.S.C. 24a(b)(2).

<sup>5</sup> See H.R. Conf. Rep. No. 106-434, at 153 (1999) ("permitting banks to affiliate with firms engaged in financial activities represents a significant expansion from the current requirement that bank affiliates may only be engaged in activities that are closely related to banking").

<sup>6</sup> See *National Courier Association v. Board of Governors of the Federal Reserve System*, 516 F.2d 1229, 1237 (D.C. Cir. 1975).

<sup>7</sup> Under the GLB Act, neither Agency may determine that an activity is financial in nature or incidental to a financial activity if the other Agency indicates in writing that it believes that the activity is not financial in nature, incidental to a financial activity, or otherwise permissible. 12 U.S.C. 1843(k)(2)(A)(ii), 24a(b)(1)(B)(i)(II).

general real estate brokerage services, several states currently permit their state-chartered banks to act as a general real estate broker.<sup>10</sup> The Office of Thrift Supervision (“OTS”) also has permitted the service corporation subsidiaries of federal savings associations to provide general real estate brokerage services.<sup>11</sup> In addition, national and state bank trust departments have long been involved as agent in the purchase and sale of real estate assets that are part of trust estates.

Although bank holding companies and financial subsidiaries do not have authority to provide real estate brokerage services, banks and bank holding companies engage in a wide variety of other real-estate related activities, including (i) holding bank premises and acquiring real estate in a fiduciary capacity or in full or partial satisfaction of a debt previously contracted; (ii) making real estate investments that have as their primary purpose community development (subject to certain limits); (iii) providing real estate appraisal services; (iv) arranging commercial real estate equity financing; (v) real estate lending; (vi) real estate leasing; (vii) providing real estate settlement and escrow services; and (viii) providing real estate investment advisory services.<sup>12</sup> Since the passage of the GLB Act, FHCs and financial subsidiaries also have been able to provide title insurance, private mortgage insurance, and any other type of insurance to the parties to a real estate transaction.<sup>13</sup> As a result, banks

and bank holding companies participate in most aspects of the typical real estate transaction other than brokerage.

In addition, banks and bank holding companies currently engage in a variety of activities that are functionally and operationally similar to real estate brokerage. Banking organizations have provided their customers with various agency transactional services, including securities brokerage services, private placement services, futures commission merchant services, agency transactional services relating to swaps and other derivative instruments, and insurance agency services.<sup>14</sup> Although these agency services are provided by banking organizations in connection with an underlying financial transaction (the purchase of securities, derivatives, or insurance), the agency services provided by a real estate broker are similar in nature to those provided by a securities, derivatives, or insurance broker.

Although the full range of real estate brokerage services would not fit within the scope of national bank or FHC finder authority,<sup>15</sup> many of the essential aspects of real estate brokerage are already permissible finder activities. The OCC’s regulations provide that “a national bank may act as a finder in bringing together a buyer and a seller” for a financial or nonfinancial transaction and further provide that permissible finder activities include “identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction that the parties themselves negotiate and consummate.”<sup>16</sup> Pursuant to the finder and financial counseling authorities, the OCC has permitted national banks to locate, analyze, and make recommendations regarding the

purchase or sale of real estate; and to place real estate investment properties by contacting a limited number of qualified investors, identifying and engaging real estate brokers, advising investors regarding the terms of a real estate sale, and administering a real estate closing.<sup>17</sup> A final rule issued by the Board on December 13, 2000, authorized FHCs to act as a finder.<sup>18</sup>

In addition, the authority of national banks and bank holding companies to assist third parties in obtaining commercial real estate equity financing includes an important subset, although not the full panoply, of services provided by the typical real estate broker.<sup>19</sup> In this regard, the Board has allowed bank holding companies to act as an intermediary for the financing of commercial or industrial income-producing real estate by arranging for the transfer of the title, control, and risk of such a real estate project to one or more investors. Bank holding companies may only arrange commercial real estate equity financing with respect to real estate projects that are not sponsored by or invested in by the holding company. The OCC similarly has authorized national banks to arrange for the placement of equity interests in commercial and investment real estate.<sup>20</sup>

In determining whether an activity is financial in nature or incidental to a financial activity, the GLB Act specifically instructs the Board and the Secretary to consider whether the activity is necessary or appropriate to allow a FHC or a bank, respectively, to compete effectively with other financial services companies operating in the United States.<sup>21</sup> Before the passage of the GLB Act, in determining whether an activity was “closely related to banking,” the law directed the Board to consider whether banks engaged in the activity, but did not explicitly authorize the Board to consider whether other financial service providers engaged in the activity.<sup>22</sup> This change in law represents a significant expansion of the

<sup>10</sup> See, e.g., Iowa Code § 524.802 (“A state bank shall have \* \* \* the power to \* \* \* engage in the brokerage of insurance and real estate subject to the prior approval of the superintendent.”); N.J. Admin. Code tit. 3, § 11–11.5(a)(4) (permitting a subsidiary of a New Jersey state-chartered bank to provide real estate brokerage services); 1979 Ky. AG LEXIS 224 (“A state bank, through its authorized trust department, and state trust companies may act as real estate brokers or salesmen in the general real estate business, regardless of whether it involves the institution’s fiducial business or not.”).

<sup>11</sup> See 12 CFR 559.4(e)(4) and OTS Letter, July 16, 1997 (1997 OTS LEXIS 3).

<sup>12</sup> With respect to bank holding companies, see, e.g., 12 CFR 225.22(d)(1) and (3) and 225.28(b)(2), (3), and (12). With respect to national banks, see, e.g., 12 U.S.C. 29 (holding bank premises and acquiring real estate DPC); 12 U.S.C. 92a (general fiduciary authority); OCC Interpretive Letter No. 467, *reprinted in* [1988–1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,691 (Jan. 24, 1989) (providing real estate appraisal services); OCC Interpretive Letter No. 387, *reprinted in* [1988–1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,611 (June 22, 1987) (arranging commercial real estate equity financing); 12 U.S.C. 371 (real estate lending); 12 CFR 5.34(e)(5)(v) (providing real estate settlement and escrow services and real estate investment advisory services).

<sup>13</sup> See 12 U.S.C. 1843(k)(4)(B), 24a(b)(1)(A)(i). The authority of a financial subsidiary to underwrite certain types of insurance is, however, limited. See 12 U.S.C. 24a(a)(2)(B)(i).

<sup>14</sup> With respect to bank holding companies, see, e.g., 12 CFR 225.28(b)(7) and 12 U.S.C. 1843(k)(4)(B). With respect to national banks, see, e.g., 12 U.S.C. 24(7) (securities brokerage services); OCC Interpretive Letter No. 329, *reprinted in* [1985–1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,499 (Mar. 4, 1985) (private placement services); 12 CFR 5.34(e)(5)(v) (futures commission merchant services and agency transactional services relating to swaps and derivatives); and 12 U.S.C. 92 (insurance agency services).

<sup>15</sup> Real estate brokerage would not fit within the finder activities permitted to national banks because real estate brokerage essentially involves the real estate broker in negotiation of the real estate transaction—a role specifically forbidden to national bank finders. See 12 CFR 7.1002(b). Real estate brokerage would not fit within the finder activities authorized for FHCs because the Board’s finder rule prohibits a finder from becoming involved in negotiation and specifically excludes any activity that would require the FHC to register or obtain a license as a real estate agent or broker. See Board press release (December 13, 2000).

<sup>16</sup> 12 CFR 7.1002.

<sup>17</sup> See OCC Interpretive Letter No. 238, *reprinted in* [1983–1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,402 (Feb. 9, 1982). The OCC also has allowed national banks to participate in the structuring and negotiation of certain real estate exchange transactions. See OCC Interpretive Letter No. 880, *reprinted in* [1999–2000 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,373 (Dec. 6, 1999).

<sup>18</sup> See Board press release (December 13, 2000).

<sup>19</sup> See, e.g., 12 CFR 225.28(b)(2)(ii).

<sup>20</sup> See OCC Interpretive Letter No. 271, *reprinted in* [1983–1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,435 (Sept. 21, 1983).

<sup>21</sup> 12 U.S.C. 1843(k)(3)(D)(i), 24a(b)(2)(D)(i).

<sup>22</sup> See *National Courier Association v. Board of Governors of the Federal Reserve System*, 516 F.2d 1229, 1237 (D.C. Cir. 1975).

Board's capacity to consider the competitive realities of the U.S. financial marketplace in determining the permissibility of activities for FHCs.

As the financial marketplace continues to evolve, it appears that many financial companies are adding real estate brokerage to their menu of services. In this regard, the ABA has provided evidence that several diversified financial companies provide real estate brokerage services in addition to their more traditional banking, securities, and insurance services.<sup>23</sup> The ABA also has asserted that buyers and sellers of real estate are increasingly looking to a single company to provide all of their real estate-related needs. Purchasers of real estate seem especially interested in obtaining real estate brokerage and mortgage finance from a single provider. The ABA argues that permitting FHCs and financial subsidiaries to engage in real estate brokerage activities would permit FHCs and banks to compete effectively with other financial service providers in the United States. The Agencies solicit comment on the extent to which U.S. financial services companies provide real estate brokerage services.

Existing federal and state laws should operate to mitigate the potential adverse effects of combining banking and real estate brokerage. The antitying rules should help prevent banks from using any market power they possess to assist an affiliated financial subsidiary or FHC in monopolizing or competing unfairly in the real estate brokerage business. The antitying rules would prohibit a subsidiary bank of a FHC engaged in real estate brokerage or the parent bank of a financial subsidiary engaged in real estate brokerage from extending credit, furnishing any service, or varying the consideration for any loan or service on the condition that the customer obtain real estate brokerage services from the bank or any affiliate (including a financial subsidiary) of the bank.<sup>24</sup> Sections 23A and 23B of the Federal Reserve Act would limit the amount of credit and certain other forms of support that a bank could provide to a real estate brokerage affiliate (including a financial subsidiary).<sup>25</sup> In addition, section 23B would require mortgage loans by a bank

to a customer who obtains real estate brokerage services from a bank affiliate (including a financial subsidiary) to be on market terms.<sup>26</sup> Furthermore, federal and state consumer protection laws, including the Real Estate Settlement Procedures Act,<sup>27</sup> would help protect customers of banks and affiliated real estate brokers. The Agencies solicit comment on the potential adverse effects of allowing FHCs or financial subsidiaries to act as a real estate broker and whether special restrictions on transactions or relationships between a real estate broker and its affiliated depository institutions are necessary to mitigate those adverse effects.<sup>28</sup>

Permitting FHCs and financial subsidiaries to engage in real estate brokerage does not appear to present significant risks to those organizations or their depository institution affiliates. The proposed rules would ensure that the authorized real estate brokerage services are agency services only and that FHCs and financial subsidiaries take no principal risk in connection with real estate transactions that they broker. As a consequence, FHCs and financial subsidiaries engaging in real estate brokerage would not be subject to either the liquidity risk or market risk associated with real estate investment and development. Real estate brokerage involves operational and legal risks, but these risks appear similar in nature and extent to those posed by other agency activities conducted by FHCs and financial subsidiaries.

## 2. Real Estate Brokerage as a Statutorily Listed Financial Activity

The ABA has argued that real estate is a financial asset and that, accordingly, the Agencies should find real estate brokerage to be part of the statutorily listed financial activity of "[l]ending, exchanging, transferring, investing for others or safeguarding financial assets

other than money or securities."<sup>29</sup> According to the ABA, real estate is a financial asset because (i) the home is the largest asset for many individuals; (ii) real estate serves as the underpinning for hundreds of billions of dollars of mortgage-backed securities; and (iii) real estate serves as a means of wealth creation by increasing in value over time and providing tax benefits.

The Agencies are not convinced that real estate should be deemed a financial asset because it is a comparatively large asset on most individuals' personal balance sheet or because it often is used as collateral for financial instruments. Airplanes, boats, and automobiles are large assets that are often used as collateral for financial instruments (loans and leases in particular), yet these assets are generally considered to be nonfinancial. The Agencies recognize, however, that real estate does have certain important attributes of a financial asset; namely, that individuals often purchase real estate, at least in part, for investment purposes and with a view toward the financial benefits of the transaction.

These financial attributes of real estate may, however, not be enough to justify treating real estate as a financial asset. Although real estate often is purchased, in part, for investment purposes, the same can be said of many nonfinancial assets such as fine art, rare stamps, and antique cars. Moreover, whereas loans, securities, and most other financial assets are held for investment purposes only, most purchasers and renters of real estate also use the property as a residence or in the operation of a business. Finally, financial assets are generally thought to include money, loans, securities, and other similar intangible properties. Real estate, on the other hand, is a tangible, physical asset.

The ABA also has argued that the purchase, sale, or lease of real estate is a financial transaction and that, accordingly, the Agencies should find that real estate brokerage is part of the listed financial activity of "[a]rranging, effecting, or facilitating financial transactions for the account of third parties."<sup>30</sup> The ABA contends that the purchase, sale, or lease of real estate is a financial transaction because it is the most important, complex, and financially difficult transaction that

<sup>26</sup> 12 U.S.C. 371c-1(a)(2)(D). Section 23A also would cover mortgage loans by a bank to a customer to the extent that the customer uses part of the loan proceeds to pay the brokerage commission of a real estate brokerage affiliate of the bank.

<sup>27</sup> 12 U.S.C. 2601 *et seq.*

<sup>28</sup> Under section 114 of the GLB Act, the Board has authority to impose restrictions or requirements on transactions or relationships between a depository institution subsidiary of a bank holding company and any affiliate of such depository institution, if the Board finds that such action would be (i) consistent with the purposes of applicable Federal law and (ii) appropriate, among other things, to avoid adverse effects such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices. GLB Act Section 114(b). Section 114 provides the OCC with similar authority to impose restrictions or requirements on transactions or relationships between a national bank and its subsidiaries. GLB Act Section 114(a).

<sup>23</sup> For example, General Motors Acceptance Corporation operates a thrift, makes mortgage loans, and provides real estate brokerage services; Prudential Insurance Company provides insurance and securities products and real estate brokerage services; Cendant Corporation provides insurance, mortgage loans, and real estate brokerage services; and Long & Foster provides mortgage loans, insurance products, and real estate brokerage services.

<sup>24</sup> 12 U.S.C. 1972(1)(B).

<sup>25</sup> 12 U.S.C. 371c and 371c-1.

<sup>29</sup> 12 U.S.C. 1843(k)(5)(B)(i), 24a(b)(3)(A). The GLB Act requires the Agencies jointly to define this activity and two other listed activities as "financial in nature" and to determine "the extent to which such activities are financial in nature or incidental to a financial activity." 12 U.S.C. 1843(k)(5)(A), 24a(b)(3).

<sup>30</sup> 12 U.S.C. 1843(k)(5)(B)(iii), 24a(b)(3)(C).

most individuals undertake. The Agencies are not convinced that the importance, complexity, or size of a transaction should affect a determination as to whether the transaction is financial in nature. On the other hand, real estate transactions often are entered into, at least in part, for investment purposes. To that extent, real estate transactions do have some aspects of a financial transaction. The Agencies seek comment on the above issues.

### 3. Arguments of the NAR

As noted, the NAR has asked that the Agencies not authorize real estate brokerage activities. The NAR makes four principal contentions in support of its position. First, the NAR notes that the GLB Act does not specifically authorize FHCs to engage in real estate brokerage. Although this contention is true, the GLB Act also authorizes each Agency to supplement the statutory activities list with additional activities that it determines, in consultation with the other Agency, to be financial in nature or incidental to a financial activity. The NAR points out that the GLB Act specifically prohibits financial subsidiaries from engaging in real estate investment and development activities, but this prohibition by its terms does not apply to FHCs or to real estate brokerage activities.

Second, the NAR suggests that it would be inappropriate for the Board now to permit FHCs to provide real estate brokerage services because the Board prohibited bank holding companies from acting as a real estate broker in 1972. As noted above, the Board's 1972 decision on real estate brokerage was made pursuant to the former "closely related to banking" standard; the GLB Act now authorizes the Board to approve any activity that is "financial in nature" or "incidental to a financial activity." The plain meaning of and legislative history behind the "financial" and "incidental to financial" standards suggest that Congress intended the new standards to be significantly broader than the old "closely related to banking" test. Furthermore, the financial services environment has changed significantly in the past 30 years, and what may have been an inappropriate activity for bank holding companies in the early 1970s may be appropriate for the diversified FHCs of the early 21st century.

Third, the NAR claims that real estate brokerage is a commercial activity and not a financial activity. Finally, the NAR argues that the Agencies should delay finding real estate brokerage to be a permissible activity until such time as

FHCs gain experience in conducting the various other new activities authorized by the GLB Act.

The Agencies seek comment on whether real estate brokerage is an activity that is financial in nature or incidental to a financial activity. In addition, the Agencies seek comment on the particular arguments advanced by the NAR.

#### B. Real Estate Management Services

Real estate management is the business of providing for others day-to-day management of real estate. Day-to-day management of real estate could include procuring tenants; negotiating leases; maintaining security deposits; billing and collecting rent payments; providing periodic accountings for such payments; making principal, interest, insurance, tax, and utilities payments; and generally overseeing inspection, maintenance, and upkeep of real property. Real estate management generally does not involve purchasing, selling, or owning real estate as principal. Although some states do not subject real estate managers to special licensing laws or regulations, real estate managers in other states are subject to the same state licensing laws and regulations that apply to real estate brokers.

The Board first proposed allowing bank holding companies to provide property management services in 1971.<sup>31</sup> For a variety of reasons, however, including the substantial volume of negative public comment received on the proposal, the Board determined in 1972 that property management was not closely related to banking for purposes of the BHC Act.<sup>32</sup> Similarly, the OCC has not permitted national banks to engage in general real estate management.<sup>33</sup>

The Agencies have some doubts as to whether all aspects of real estate management are financial in nature or incidental to a financial activity. The Agencies also are concerned that certain forms of real estate management appear to resemble more closely day-to-day operation of a commercial enterprise than serving as the intermediary between the owners and users of real estate. Nevertheless, for the reasons discussed below, the Agencies believe

<sup>31</sup> See 36 FR 18427 (Sept. 7, 1971).

<sup>32</sup> 12 CFR 225.126(g); 58 Federal Reserve Bulletin 652 (1972). As part of the 1987 Proposal, the Board proposed authorizing a bank holding company to provide real estate management services in connection with real estate in which the bank holding company had an interest. See 52 FR 543 (Nov. 4, 1987); see also 50 FR 4519 (Jan. 31, 1985). As noted above, the Board never finalized this proposed rule.

<sup>33</sup> See OCC Interpretive Letter No. 238, *supra*.

that they should seek public comment on (i) what activities are included within real estate management and (ii) which of these activities, if any, are financial in nature or incidental to a financial activity within the meaning of section 4(k)(1)(A) of the BHC Act and section 5136A(a)(2)(A)(i) of the Revised Statutes.

#### 1. General "Financial in Nature or Incidental" Analysis

Neither the OCC nor state banking departments, to the Agencies' knowledge, have permitted banks to provide general real estate management services. Thrift holding companies (including non-unitary thrift holding companies) and thrift service corporation subsidiaries, however, have been permitted to maintain and manage real estate.<sup>34</sup> In addition, as noted above, banking organizations have long been engaged in a variety of real estate-related activities. Moreover, some (though not all) real estate management activities appear to be functionally and operationally similar to various other activities that banks and bank holding companies currently engage in. For example, collecting rental payments; maintaining security deposits; making principal, interest, taxes, and insurance payments; and providing periodic accountings are functionally similar to collecting loan or lease payments, disbursing escrow payments, and performing related accountings. In addition, banks and bank holding companies have a long history of managing real estate assets that are part of trust estates, that are used by the banking organization in its own operations, or that are acquired as a result of foreclosure.<sup>35</sup>

As noted above, in determining whether an activity is financial in nature or incidental to a financial activity, the GLB Act instructs the Board and the Secretary to consider whether the activity is necessary or appropriate to allow FHCs or banks, respectively, to compete effectively with other financial services companies operating in the United States. The ABA has contended that competitive considerations support a determination to allow FHCs and financial subsidiaries to provide real estate management services. The Agencies solicit comment on the extent to which financial services companies

<sup>34</sup> See 12 CFR 559.4(e)(3), 584.2-1(b)(8).

<sup>35</sup> See, e.g., OCC Interpretive Letter No. 238, *supra*; OCC Interpretive Letter No. 355, *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,525 (Dec. 10, 1985); *Bancorp Hawaii, Inc.*, 71 Federal Reserve Bulletin 168, 168 n.2 (1985); *United Missouri Bancshares, Inc.*, 64 Federal Reserve Bulletin 415, 417 (1978).

provide real estate management services in the United States and on whether permitting FHCs and financial subsidiaries to provide real estate management services would help ensure competitive equity between FHCs and financial subsidiaries and other financial firms.

The same laws that would operate to mitigate potential adverse effects in the real estate brokerage context also would help to alleviate adverse effects in the provision of real estate management services. The Agencies solicit comment on the potential adverse effects of allowing FHCs and financial subsidiaries to act as a real estate manager and whether special restrictions are necessary to mitigate those adverse effects.

Permitting FHCs and financial subsidiaries to engage in real estate management activities does not appear to present significant risks to those organizations or their depository institution affiliates. The proposed rules would ensure that the authorized real estate management services are agency services only and that FHCs and financial subsidiaries take no principal risk in connection with real estate that they manage. The Agencies recognize, however, that engaging in property management may increase the operational, legal, and reputational risks faced by a FHC or financial subsidiary. Accordingly, the Agencies seek comment on the nature and extent of these risks.

## 2. Real Estate Management as a Statutorily Listed Financial Activity

The ABA has argued that the Agencies should find that real estate management is part of the listed financial activity of “[l]ending, exchanging, transferring, investing for others or safeguarding financial assets other than money or securities.”<sup>36</sup> If the Agencies were to conclude that real estate is a financial asset, this argument would have some textual appeal. Real estate management could be viewed, in part, as a form of safeguarding real estate.

The ABA also has argued that the Agencies should find that real estate management services are part of the listed financial activity of “[a]rranging, effecting, or facilitating financial transactions for the account of third parties.”<sup>37</sup> Part of the role of a property manager does involve the facilitation of financial transactions: For example, maintenance of security deposits, collection of rent payments, and

distribution of principal, interest, insurance, tax, and utility payments. Property management also, however, appears to have components that go beyond the facilitation of financial transactions. The Agencies seek comment on the above issues.

### C. Description of the Proposed Rules

#### 1. Real Estate Brokerage

The proposed rules authorize FHCs and financial subsidiaries to provide real estate brokerage services and include examples of the sorts of activities that the Agencies consider to be included within real estate brokerage. The Agencies seek comment on whether any final rules should provide further guidance regarding the scope of activities that are included within real estate brokerage.

Importantly, the proposed rules also contain restrictions designed to ensure that a FHC or financial subsidiary, when acting as a real estate broker, serves only as an intermediary between buyers and sellers (or lessees and lessors) and does not otherwise become impermissibly involved in the underlying real estate transaction. In particular, the proposed rules make clear that they do not authorize a FHC or financial subsidiary to (i) invest in or develop real estate; or (ii) take title to, acquire, or hold an ownership interest in any real estate that is the subject of the company’s real estate brokerage services.

The Agencies understand that many real estate brokers offer employee relocation services to their corporate clients. Certain fundamental employee relocation services—assisting a client’s transferred employees to sell their existing homes, buy homes in their destination locations, and obtain mortgage financing for their new home purchases—appear to be forms of real estate brokerage or currently permissible financial activities.

Other employee relocation activities seem less obviously a part of real estate brokerage or otherwise financial in nature. For example, a real estate broker providing employee relocation services often commits to purchase any home owned by one of its client’s transferred employees at a fixed price if the broker fails to sell the home within a certain time period. The Agencies believe that such services may be incidental to real estate brokerage if the homes purchased by the broker are sold within a short time period, the broker’s total holdings of unsold real estate do not exceed some threshold amount, and the broker only purchases unsold real estate in connection with providing bona fide employee relocation services to

customers (not for the purpose of speculating on the price of real estate). The Agencies also understand that employee relocation services often include assisting transferred employees to move household goods to their destination locations and assisting the spouses of transferred employees to find employment in their destination locations.

The Agencies request information on the kinds of employee relocation services that real estate brokers currently provide. The Agencies also seek comment on whether to permit FHCs or financial subsidiaries: (i) To provide employee relocation services as part of real estate brokerage or otherwise; (ii) to purchase residential real estate in connection with providing employee relocation services and, if so, what conditions or limits should apply to such real estate purchases; and (iii) to assist transferred employees to move their household goods and to assist the spouses of transferred employees to find employment in connection with providing employee relocation services.

#### 2. Real Estate Management

The proposed rules authorize FHCs and financial subsidiaries to provide real estate management services and include examples of the sorts of activities that the Agencies consider to be included within real estate management.

The ABA has suggested that the Agencies’ definition of real estate management should include any activities that may be defined as “real estate management” under any state law. The Agencies generally are reluctant to delegate to state legislatures any determinations regarding the scope of permissible activities for federally regulated banking organizations. Nevertheless, the Agencies specifically solicit comment on whether real estate management activities should be defined explicitly to include any activities that are defined as “real estate management” under state law. The Agencies also request comment more generally on whether any final rules should contain further guidance regarding the scope of activities that are included within real estate management.

The proposed rules contain restrictions designed to ensure that a FHC or financial subsidiary, when providing real estate management services, acts only in an agency capacity as an intermediary between the owners and users of real estate. In particular, the proposed rules make clear that real estate management does not include (i) investing in or developing real estate; or

<sup>36</sup> 12 U.S.C. 1843(k)(5)(B)(i), 24a(b)(3)(A).

<sup>37</sup> 12 U.S.C. 1843(k)(5)(B)(iii), 24a(b)(3)(C).

(ii) taking title to, acquiring, or holding an ownership interest in any real estate that the FHC or financial subsidiary manages. In light of these exclusions, the Agencies request comment on whether real estate managers receive compensation in the form of an equity or equity-like interest in the managed real estate and, if so, whether the Agencies should prevent FHCs that engage in real estate management from receiving compensation in this form.

The proposed rules also prevent a FHC or financial subsidiary that provides real estate management services from itself repairing or maintaining the managed real estate. The Agencies have doubts as to whether repair and maintenance of real estate are activities that are financial in nature or incidental to a financial activity. The proposed rules allow a FHC or financial subsidiary, however, to arrange for a third party to provide these services. The Agencies request comment on whether FHCs and financial subsidiaries should be limited in their authority to engage in any other aspects of real estate management.

The Agencies also seek comment on whether they should draw any distinctions between the management of single-family housing, multi-family housing, office buildings, institutional buildings (hotels, hospitals, etc.), commercial and industrial properties, and farms. In addition, the Agencies solicit comment on whether real estate management should include management of the air rights above and the oil and mineral rights beneath particular parcels of land. As noted above, the Agencies are concerned that certain forms of real estate management may more closely resemble day-to-day operation of a commercial enterprise than serving as the intermediary between the owners and users of real estate.

#### Plain Language

Section 722 of the GLB Act requires the Board to use "plain language" in all proposed and final rules published after January 1, 2000. In light of this requirement, the Board has sought to present its proposed rule in a simple and straightforward manner and has included in the rule examples of activities that would be permissible under the proposed rule. The Board invites comments on whether there are additional steps the Board could take to make the proposed rule easier to understand.

#### Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act, the Agencies

certify that the proposed rules would not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). The proposed rules would remove regulatory restrictions on financial holding companies and financial subsidiaries of national banks by permitting them to engage in real estate brokerage and real estate management activities. The proposed rules would apply to all financial holding companies and national bank financial subsidiaries, regardless of their size. The proposed rules should enhance the ability of financial holding companies and financial subsidiaries, including small financial holding companies and financial subsidiaries, to compete with other providers of financial services in the United States and to respond to technological and other changes in the marketplace in which they compete. Accordingly, a regulatory flexibility analysis is not required.

#### Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR part 1320 Appendix A.1), the Board has reviewed the proposed rule under the authority delegated to the Board by the Office of Management and Budget. No collections of information pursuant to the Paperwork Reduction Act are contained in the proposed rule.

#### List of Subjects

##### 12 CFR Part 225

Administrative practice and procedures, Banks, Banking, Federal Reserve System, Holding companies, Reporting and recordkeeping requirements, Securities.

##### 12 CFR Part 1501

Administrative practice and procedure, National Banks, Reporting and recordkeeping requirements.

#### Federal Reserve System

##### 12 CFR Chapter II

#### Authority and Issuance

For the reasons set forth in the joint preamble, part 225 of chapter II, title 12 of the Code of Federal Regulations is proposed to be amended as follows:

#### PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL (REGULATION Y)

1. The authority citation for part 225 continues to read as follows:

**Authority:** 12 U.S.C. 1817(j)(13), 1818, 1828(o), 1831i, 1831p-1, 1843(c)(8), 1843(k),

1844(b), 1972(l), 3106, 3108, 3310, 3331-3351, 3907, and 3909.

2. Section 225.86(d), published at 65 FR 80740, December 22, 2000, is amended by adding new paragraphs (d)(2) and (d)(3) to read as follows:

#### § 225.86 What activities are permissible for financial holding companies?

\* \* \* \* \*

(d) \* \* \*

(2) *Real estate brokerage.*

(i) Providing real estate brokerage services, including, among other things, acting as an agent for a buyer, seller, lessor, or lessee of real estate; listing and advertising real estate; providing advice in connection with a real estate purchase, sale, exchange, lease, or rental transaction; bringing together parties interested in consummating such a real estate transaction; and negotiating on behalf of such parties a contract relating to such a real estate transaction.

(ii) In providing real estate brokerage services, a financial holding company may not:

(A) Invest in or develop real estate as principal; or

(B) Take title to, acquire, or hold any ownership interest in real estate brokered by the company.

(3) *Real estate management.*

(i) Providing real estate management services, including, among other things, procuring tenants; negotiating leases; maintaining security deposits; billing and collecting rent payments; providing periodic accountings for such payments; making principal, interest, insurance, tax, and utility payments; and generally overseeing the inspection, maintenance, and upkeep of real estate.

(ii) In providing real estate management services, a financial holding company may not:

(A) Invest in or develop real estate as principal;

(B) Take title to, acquire, or hold any ownership interest in real estate managed by the company; or

(C) Directly or indirectly maintain or repair real estate managed by the company (but may arrange for a third party to provide these services).

By order of the Board of Governors of the Federal Reserve System, December 26, 2000.

**Jennifer J. Johnson,**  
*Secretary of the Board.*

#### Department of the Treasury

##### 12 CFR Chapter XV

#### Authority and Issuance

For the reasons set forth in the joint preamble, part 1501 of chapter XV, title 12 of the Code of Federal Regulations is proposed to be amended as follows:

## PART 1501—FINANCIAL SUBSIDIARIES

1. The authority citation for part 1501 continues to read as follows:

**Authority:** 12 U.S.C. 24a.

2. Section 1501.2, published in an interim rule in this issue of the **Federal Register**, is amended by adding new paragraphs (b) and (c) to read as follows:

### 1501.2 What activities has the Secretary determined to be financial in nature or incidental to a financial activity?

(a) \* \* \*

(b) *Real estate brokerage.*

(1) Providing real estate brokerage services, including, among other things, acting as an agent for a buyer, seller, lessor, or lessee of real estate; listing and advertising real estate; providing advice in connection with a real estate purchase, sale, exchange, lease, or rental transaction; bringing together parties interested in consummating such a real estate transaction; and negotiating on behalf of such parties a contract relating to such a real estate transaction.

(2) In providing real estate brokerage services, a financial subsidiary may not:

(i) Invest in or develop real estate as principal; or

(ii) Take title to, acquire, or hold any ownership interest in real estate brokered by the financial subsidiary.

(c) *Real estate management.*

(1) Providing real estate management services, including, among other things, procuring tenants; negotiating leases; maintaining security deposits; billing and collecting rent payments; providing periodic accountings for such payments; making principal, interest, insurance, tax, and utility payments; and generally overseeing the inspection, maintenance, and upkeep of real estate.

(2) In providing real estate management services, a financial subsidiary may not:

(i) Invest in or develop real estate as principal;

(ii) Take title to, acquire, or hold any ownership interest in real estate managed by the financial subsidiary; or

(iii) Directly or indirectly maintain or repair real estate managed by the financial subsidiary (but may arrange for a third party to provide these services).

Dated: December 26, 2000.

**Gregory A. Baer,**

*Assistant Secretary for Financial Institutions,*  
*Department of the Treasury.*

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## RAILROAD RETIREMENT BOARD

### 20 CFR Part 369

**RIN 3220-AB49**

### Use of the Seal of the Railroad Retirement Board

**AGENCY:** Railroad Retirement Board.

**ACTION:** Proposed rule.

**SUMMARY:** The Railroad Retirement Board (Board) proposes to amend its regulations to add a part explaining when use of the Board's seal is permitted. Federal law prohibits the use of an agency seal except as authorized by regulation. The Board currently has no such regulation.

**DATE:** Comments should be submitted on or before March 5, 2001.

**ADDRESSES:** Any comments should be submitted to the Secretary to the Board, Railroad Retirement Board, 844 North Rush Street, Chicago, IL 60611.

**FOR FURTHER INFORMATION CONTACT:** Marguerite P. Dabado, Assistant General Counsel, Railroad Retirement Board, (312) 751-4945, TDD (312) 751-4701.

**SUPPLEMENTARY INFORMATION:** The Railroad Retirement Board is an independent agency in the executive branch of the United States Government which is charged with the administration of the Railroad Retirement Act (45 U.S.C. 231 *et seq.*) and the Railroad Unemployment Insurance Act (45 U.S.C. 351 *et seq.*). Use of agency seals is governed by 18 U.S.C. 701 which prohibits the use of agency seals except as authorized under regulations made pursuant to law. This proscription is intended to protect the public against the use of a recognizable assertion of authority with intent to deceive (*U.S. v. Goeltz*, 513 F.2d 193 (C.A. Utah 1975), *cert. den.* 423 U.S. 830). The regulations of the Railroad Retirement Board do not include provisions for the authorization of use of the Agency's seal. The Board proposes to add Part 369 to its regulations to explain when use of the Board's seal is permitted.

In order to comply with the President's June 1, 1998, memorandum directing the use of plain language for all proposed and final rulemaking, the regulatory paragraphs introduced by the above rule changes have been written in plain language.

This rule concerns agency management and is not a regulation as defined in Executive Order 12866. Therefore, no regulatory impact analysis is required. There are no information collections associated with this rule.

## List of Subjects in 20 CFR Part 369

Railroad retirement, Seals and insignia.

For the reasons set out in the preamble, the Railroad Retirement Board proposes to add part 369 to title 20, chapter II of the Code of the Federal Regulations to read as follows:

### PART 369—USE OF THE SEAL OF THE RAILROAD RETIREMENT BOARD

Sec.

369.1 Unofficial use of the seal of the Railroad Retirement Board.

369.2 Authority to grant written permission for use of the seal.

369.3 Procedures for obtaining permission to use the seal.

369.4 Inappropriate use of the seal.

369.5 Penalty for misuse of the seal.

**Authority:** 18 U.S.C. 701; 45 U.S.C. 231f.

#### § 369.1 Unofficial use of the seal of the Railroad Retirement Board.

Use of the seal of the Railroad Retirement Board for non-agency business is prohibited unless permission for use of the seal has been obtained in accordance with this part.

#### § 369.2 Authority to grant written permission for use of the seal.

The Board hereby delegates authority to grant written permission for the use of the seal of the Railroad Retirement Board to the Director of Administration.

#### § 369.3 Procedures for obtaining permission to use the seal.

Requests for written permission to use the seal of the Railroad Retirement Board shall be in writing and shall be directed to the Director of Administration of the Railroad Retirement Board. The request should, at a minimum, contain the following information:

(a) Name and address of the requester.

(b) A description of the type of activity in which the requester is engaged or proposes to engage.

(c) A statement of whether the requester considers the proposed use or imitation to be commercial or non-commercial, and why.

(d) A brief description and illustration or sample of the proposed use, as well as a description of the product or service in connection with which it will be used. This description will provide sufficient detail to enable the Director of Administration to determine whether the intended use of the seal is consistent with the interests of the government.

(e) In the case of a non-commercial use, a description of the requesting organization's function and purpose shall be provided.