



## Federal Reserve Finalizes Key Definition to Be Used in Making “SIFI” Designations

*Final Rule Lists Activities that Are Considered “Financial” for Purposes of Determining Whether a Nonbank Company May Be Designated as “Systemically Important” Under the Dodd-Frank Act; Final Rule Is Also Relevant to Form PF Filers*

*April 15, 2013*

The Federal Reserve recently issued a final rule defining what it means for a nonbank company to be “predominantly engaged in financial activities.”<sup>1</sup> The term is a necessary analytical component to the Financial Stability Oversight Council’s (the “FSOC”) designation of nonbank companies as “systemically important” under the Dodd-Frank Act. In addition to being predominantly engaged in financial activities, a nonbank firm designated by the FSOC must meet other criteria that would lead regulators to conclude its failure could threaten the financial stability of the United States. Such companies, known more commonly as SIFIs, will be subject to Federal Reserve supervision and regulation, as well as prudential standards provided under the Dodd-Frank Act, such as risk-based capital requirements, leverage limits, liquidity requirements, resolution planning and credit exposure report requirements, concentration limits, and short-term debt limits.<sup>2</sup>

The final rule represents another step by the FSOC to establish the groundwork for its initial designation of SIFIs. It follows the FSOC’s final rule from April 2012 setting forth the three-stage process by which the FSOC will make SIFI designations. To date, the FSOC has not made a SIFI designation with respect to a nonbank company, although a few companies have publicly disclosed that they are under review by the FSOC for designation.

The final rule also adopts other definitions relating to the relationships that nonbank financial companies have with large counterparties. Such relationships are a factor in SIFI designations.

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<sup>1</sup> See 78 Fed. Reg. 20756 (Apr. 5, 2013) (adding Regulation PP, 12 C.F.R. Part 242: Definitions Relating to Title I of the Dodd-Frank Act).

<sup>2</sup> In December 2011, the Federal Reserve issued a proposal setting forth the enhanced prudential standards and early remediation framework that will apply to nonbank financial companies designated by the FSOC as SIFIs. See 77 Fed. Reg. 594 (Jan. 5, 2012). For more information regarding the proposal, which remains pending, please see our memorandum, titled “Regulating Systemically Important Financial Companies,” dated January 10, 2013, available at <http://www.simpsonthacher.com/siteContent.cfm?contentID=4&itemID=75&focusID=1356>.

## A. “PREDOMINANTLY ENGAGED IN FINANCIAL ACTIVITIES”

The Dodd-Frank Act provides a statutory definition establishing that a company is “predominantly engaged in financial activities” if activities that are “financial in nature,” as defined in Section 4(k) of the Bank Holding Company Act of 1956 (the “BHC Act”), account for 85% or more of the annual gross revenues derived by, or the consolidated assets of, the company and its subsidiaries (including any depository institution subsidiaries).

The final rule clarifies the definition of “predominantly engaged in financial activities” in three respects. First, the final rule sets forth mechanics of calculating the 85% threshold. A company’s consolidated annual gross financial revenues or consolidated total financial assets will account for 85% or more of its annual gross revenues or consolidated assets, respectively, if the threshold is met in either of the past two completed fiscal years, based on consolidated financial statements and using GAAP, IFRS, or other FSOC-approved accounting standards. The final rule also authorizes the FSOC or the Federal Reserve to determine, based on all the facts and circumstances, that a company meets the 85% threshold under either the gross revenues or consolidated assets and without regard to the two-year limitation.

Second, the final rule provides rules of construction to determine whether assets or revenues are related to activities that are financial in nature. Investments in unconsolidated subsidiaries are presumed to be made in the course of conducting financial activities. To avoid capturing strategic nonfinancial business ventures in unconsolidated subsidiaries (such as a joint venture to engage in business relating to a nonfinancial company’s primary business), this presumption may be rebutted with evidence that the investment is not a merchant banking investment, an investment for others, an investment in a company engaged in activities that are financial in nature, or is not otherwise related to a financial activity.

Cash is excluded from consolidated total financial assets and consolidated total assets because third parties would not be able to attribute cash to particular activities. Cash equivalents represent investments and thus are included as assets related to financial activity for purposes of the asset test. Intangible assets are treated as financial assets to the extent the transactions or assets giving rise to the intangible assets are financial assets. Accounts receivables are presumed to be assets related to the financial activity of extending credit; however, this presumption may be rebutted with evidence to the contrary.

Third, the final rule clarifies the scope of financial activities by adopting a list of activities, as set forth in the annex to this memorandum, that are considered to be “financial in nature.” These activities include, among others:

- extending credit and servicing loans;
- activities related to extending credit;
- leasing personal or real property;
- operating nonbank depository institutions (such as industrial loan companies and industrial banks, credit card banks, and thrifts);

- trust company functions;
- financial and investment advisory activities;
- agency transactional services for customer investments;
- engaging in investment transactions as principal;
- management consulting and counseling activities;
- insurance agency and underwriting;
- money orders, savings bonds and traveler's checks;
- data processing services and related activities with respect to financial, banking, or economic data;
- mutual fund administration;
- owning shares of a securities exchange;
- check cashing and wire transmission; and
- services offered in connection with banking services.

Notably, private equity funds and hedge funds, mutual funds, and investment companies (and their advisors and managers) would be deemed engaged in financial activities, as would insurance companies. Engaging in physically settled derivatives transactions generally will not be considered a financial activity. Additionally, management consulting advice provided to a client that a company owns or controls will not be considered financial activity of the company.

The statutory definition in the Dodd-Frank Act provides that "activities that are financial in nature" are those activities listed in Section 4(k) of the BHC Act. Section 4(k) includes a list of activities permitted for bank holding companies ("BHCs") that qualify as financial holding companies ("FHCs"), and also incorporates by reference activities that Federal Reserve rules have permitted for BHCs. The activities expressly listed in Section 4(k) do not precisely overlap with the activities permitted by the Federal Reserve pursuant to Regulation Y, some of which impose conditions on BHCs that are not FHCs. In addition, Section 4(k) and Regulation Y contain certain conditions applicable to FHCs and BHCs that engage in some of the permissible activities that were designed to address "safety and soundness" concerns, thus creating ambiguity as to the statutory definition's reference to Section 4(k).

The final rule resolves this ambiguity by adopting only those conditions in Section 4(k) and Regulation Y that define the financial activity itself and not those conditions imposed on the financial activity for safety and soundness reasons. For example, the condition allowing BHCs to engage in derivative transactions that are cash-settled but not physically-settled distinguishes derivative transactions conducted by financial intermediaries from those conducted by other companies, and thus defines the financial activity itself. The Federal Reserve reasoned that the inclusion of safety and soundness conditions in the definition of "activities that are financial in nature" would have allowed nonbank companies to evade Federal Reserve supervision by altering the manner in which they conduct financial activities to intentionally fail to comply with those conditions. By not incorporating certain conditions in Section 4(k) and Regulation Y,

the final rule expands the set of activities that can trigger SIFI designation, as compared to the FSOC's initial proposal.

## B. "SIGNIFICANT NONBANK FINANCIAL COMPANY" AND "SIGNIFICANT BANK HOLDING COMPANY"

The final rule also defines the terms "significant nonbank financial company" and "significant bank holding company." These terms are important because the FSOC must consider the relationships of a nonbank financial company with "significant nonbank financial companies" and "significant bank holding companies" when determining when to designate a company as a SIFI. Nonbank financial companies and BHCs with \$50 billion or more of total consolidated assets must file credit reports that describe their exposure to such companies.<sup>3</sup>

The final rule defines a "significant nonbank financial company" as any nonbank financial company supervised by the Federal Reserve and any other nonbank financial company that had \$50 billion or more in total consolidated assets as of the end of the most recently completed fiscal year. It defines a "significant bank holding company" as any BHC or company treated in the United States as a BHC with \$50 billion or more in total consolidated assets as of the end of the most recently completed calendar year, as reported on applicable Federal Reserve forms. Under both definitions, total consolidated assets equal a company's worldwide consolidated assets calculated in accordance with GAAP, IFRS or other appropriate accounting standards.

## C. SIFI DESIGNATIONS AHEAD

In April 2012, the FSOC issued a final rule and interpretive guidance setting forth the three-stage process that it will use to identify nonbank financial companies for designation as SIFIs in non-emergency situations.<sup>4</sup> Although no SIFI designations of nonbank financial companies have been made to date, the FSOC has considered an unspecified number of companies for advancement to the third and final stage of its designation process. At a meeting held on September 28, 2012, the FSOC authorized the advancement of an initial set of so-called "Stage 3" companies. These companies received written notice by the FSOC that they are under consideration, and at least three companies publicly disclosed in their securities filings that they had been so notified.

Since the initial advancement of these Stage 3 companies, the FSOC has made advancements of additional companies into Stage 3, accordingly to minutes of the FSOC's meeting held on October 18, 2012. Minutes of meetings held on January 31, 2013 and February 28, 2013 indicate that the FSOC is continuing to analyze Stage 3 companies and that FSOC members have received updates regarding the process and timing on possible proposed designations.<sup>5</sup> While

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<sup>3</sup> The status of a nonbank financial company as "significant" is distinct from a designation of such company as a SIFI.

<sup>4</sup> See 77 Fed. Reg. 21637 (Apr. 11, 2012).

<sup>5</sup> Minutes of the FSOC's meetings may be accessed through the website of the U.S. Department of the Treasury. See FSOC Meeting Minutes, available at <http://www.treasury.gov/initiatives/fsoc/council-meetings/Pages/meeting-minutes.aspx>.

the precise timing of SIFI designations remains unclear, Mary Miller, the Under Secretary for Domestic Finance of the U.S. Treasury Department, stated last month that the FSOC is in the “final stages” of evaluating the initial set of Stage 3 companies and that it is Treasury’s “hope that the [FSOC] will vote on designations in the next few months.”<sup>6</sup>

#### D. FORM PF REPORTING

Although the final rule does not discuss Form PF reporting, it is important to note that the finalized definition of “predominantly engaged in financial activities” is also relevant to investment advisors of private equity funds and hedge funds, as well as certain commodity pool operators and commodity trading advisors, that are subject to Form PF reporting. Form PF is a new reporting form, authorized under the Dodd-Frank Act, that requires filers to provide information regarding, among other things, their “financial industry portfolio companies.” Form PF defines such companies to include “nonbank financial compan[ies], as defined in [Title I of the Dodd-Frank Act].”<sup>7</sup> Accordingly, the activities listed in the annex to this memorandum will be relevant to the analysis performed by Form PF filers relating to which of their portfolio companies constitute “financial industry portfolio companies.”

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For more information regarding the final rule or the SIFI designation process, please contact a member of Simpson Thacher’s Financial Institutions Group.

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<sup>6</sup> Mary Miller, Under Secretary for Domestic Finance, U.S. Department of the Treasury, Remarks at the Annual Washington Conference of the Institute of International Bankers (Mar. 4, 2013), available at <http://www.treasury.gov/press-center/press-releases/Pages/jl1868.aspx>.

<sup>7</sup> The term “nonbank financial company” in Title I of the Dodd-Frank Act includes a nonbank company that is “predominantly engaged in financial activities.” See Dodd-Frank Act, § 102 (codified at 12 U.S.C. § 5311).



ANNEX

## FINANCIAL ACTIVITIES FOR PURPOSES OF TITLE I OF THE DODD-FRANK ACT

1. Lending, exchanging, transferring, investing for others, or safeguarding money or securities.
2. Insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker for purposes of the foregoing, in any state.
3. Providing financial, investment, or economic advisory services, including advising an investment company (as defined in Section 3 of the Investment Company Act of 1940).
4. Issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly.
5. Underwriting, dealing in, or making a market in securities.
6. Extending credit and servicing loans. Making, acquiring, brokering, or servicing loans or other extensions of credit (including factoring, issuing letters of credit and accepting drafts) for the company's account or for the account of others.
7. Activities related to extending credit. Any activity usual in connection with making, acquiring, brokering or servicing loans or other extensions of credit, including the following activities:
  - (i) Real estate and personal property appraising. Performing appraisals of real estate and tangible and intangible personal property, including securities.
  - (ii) Arranging commercial real estate equity financing. Acting as 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.
  - (iii) Check-guaranty services. Authorizing a subscribing merchant to accept personal checks tendered by the merchant's customers in payment for goods and services, and purchasing from the merchant validly authorized checks that are subsequently dishonored.
  - (iv) Collection agency services. Collecting overdue accounts receivable, either retail or commercial.
  - (v) Credit bureau services. Maintaining information related to the credit history of consumers and providing the information to a credit grantor who is considering a borrower's application for credit or who has extended credit to the borrower.

- (vi) Asset management, servicing, and collection activities. Engaging under contract with a third party in asset management, servicing, and collection<sup>1</sup> of assets of a type that an insured depository institution may originate and own.
  - (vii) Acquiring debt in default. Acquiring debt that is in default at the time of acquisition.
  - (viii) Real estate settlement servicing. Providing real estate settlement services.<sup>2</sup>
8. Leasing personal or real property. Leasing personal or real property or acting as agent, broker, or adviser in leasing such property if:
- (i) The lease is on a nonoperating basis;<sup>3</sup>
  - (ii) The initial term of the lease is at least 90 days; and
  - (iii) In the case of leases involving real property:
    - (A) At the inception of the initial lease, the effect of the transaction will yield a return that will compensate the lessor for not less than the lessor's full investment in the property plus the estimated total cost of financing the property over the term of the lease from rental payments, estimated tax benefits, and the estimated residual value of the property at the expiration of the initial lease; and
    - (B) The estimated residual value of property for purposes of the immediately preceding paragraph shall not exceed 25% of the acquisition cost of the property to the lessor.

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<sup>1</sup> Asset management services include acting as agent in the liquidation or sale of loans and collateral for loans, including real estate and other assets acquired through foreclosure or in satisfaction of debts previously contracted.

<sup>2</sup> For purposes of this section, real estate settlement services do not include providing title insurance as principal, agent, or broker.

<sup>3</sup> The requirement that the lease is on a nonoperating basis means that the company does not, directly or indirectly, engage in operating, servicing, maintaining, or repairing leased property during the lease term. For purposes of the leasing of automobiles, the requirement that the lease is on a nonoperating basis means that the company does not, directly or indirectly: (1) provide servicing, repair, or maintenance of the leased vehicle during the lease term; (2) purchase parts and accessories in bulk or for an individual vehicle after the lessee has taken delivery of the vehicle; (3) provide the loan of an automobile during servicing of the leased vehicle; (4) purchase insurance for the lessee; or (5) provide for the renewal of the vehicle's license merely as a service to the lessee where the lessee could renew the license without authorization from the lessor.

9. Operating nonbank depository institutions.
  - (i) Industrial banking. Owning, controlling, or operating an industrial bank, Morris Plan bank, or industrial loan company that is not a bank for purposes of the BHC Act.
  - (ii) Operating savings associations. Owning, controlling, or operating a savings association.
10. Trust company functions. Performing functions or activities that may be performed by a trust company (including activities of a fiduciary, agency, or custodial nature), in the manner authorized by federal or state law that is not a bank for purposes of Section 2(c) of the BHC Act.
11. Financial and investment advisory activities. Acting as investment or financial advisor to any person, including (without, in any way, limiting the foregoing):
  - (i) Serving as investment adviser (as defined in Section 2(a)(20) of the Investment Company Act of 1940, 15 U.S.C. § 80a-2(a)(20)), to an investment company registered under that act, including sponsoring, organizing, and managing a closed-end investment company;
  - (ii) Furnishing general economic information and advice, general economic statistical forecasting services, and industry studies;
  - (iii) Providing advice in connection with mergers, acquisitions, divestitures, investments, joint ventures, leveraged buyouts, recapitalizations, capital structurings, financing transactions and similar transactions, and conducting financial feasibility studies;<sup>4</sup>
  - (iv) Providing information, statistical forecasting, and advice with respect to any transaction in foreign exchange, swaps, and similar transactions, commodities, and any forward contract, option, future, option on a future, and similar instruments;
  - (v) Providing educational courses, and instructional materials to consumers on individual financial management matters; and
  - (vi) Providing tax-planning and tax-preparation services to any person.

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<sup>4</sup> Feasibility studies do not include assisting management with the planning or marketing for a given project or providing general operational or management advice.



12. Agency transactional services for customer investments.

- (i) Securities brokerage. Providing securities brokerage services (including securities clearing and/or securities execution services on an exchange), whether alone or in combination with investment advisory services, and incidental activities (including related securities credit activities and custodial services).
- (ii) Riskless principal transactions. Buying and selling in the secondary market all types of securities on the order of customers as a “riskless principal” to the extent of engaging in a transaction in which the company, after receiving an order to buy (or sell) a security from a customer, purchases (or sells) the security for its own account to offset a contemporaneous sale to (or purchase from) the customer.
- (iii) Private placement services. Acting as agent for the private placement of securities in accordance with the requirements of the Securities Act of 1933 and the rules of the Securities and Exchange Commission.
- (iv) Futures commission merchant. Acting as a futures commission merchant for unaffiliated persons in the execution, clearance, or execution and clearance of any futures contract and option on a futures contract.
- (v) Other transactional services. Providing to customers as agent transactional services with respect to swaps and similar transactions, any transaction described in paragraph 12(vi) (Investment transactions as principal) below, any transaction that is permissible for a state member bank, and any other transaction involving a forward contract, option, futures, option on a futures or similar contract (whether traded on an exchange or not) relating to a commodity that is traded on an exchange.

13. Investment transactions as principal.

- (i) Underwriting and dealing in government obligations and money market instruments. Underwriting and dealing in obligations of the United States, general obligations of states and their political subdivisions, and other obligations that state member banks of the Federal Reserve System may be authorized to underwrite and deal in under 12 U.S.C. §§ 24 and 335, including banker’s acceptances and certificates of deposit.
- (ii) Investing and trading activities. Engaging as principal in:
  - (A) Foreign exchange;
  - (B) Forward contracts, options, futures, options on futures, swaps, and similar contracts, whether traded on exchanges or not, based on any

rate, price, financial asset (including gold, silver, platinum, palladium, copper, or any other metal), nonfinancial asset, or group of assets, other than a bank-ineligible security,<sup>5</sup> if:

- (1) A state member bank is authorized to invest in the asset underlying the contract;
  - (2) The contract requires cash settlement;
  - (3) The contract allows for assignment, termination, or offset prior to delivery or expiration, and the company makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract or receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset; or
  - (4) The contract does not allow for assignment, termination, or offset prior to delivery or expiration and is based on an asset for which futures contracts or options on futures contracts have been approved for trading on a U.S. contract market by the Commodity Futures Trading Commission, and the company makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract or receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset.
- (C) Forward contracts, options,<sup>6</sup> futures, options on futures, swaps, and similar contracts, whether traded on exchanges or not, based on an index of a rate, a price, or the value of any financial asset, nonfinancial asset, or group of assets, if the contract requires cash settlement.
- (iii) Buying and selling bullion, and related activities. Buying, selling and storing bars, rounds, bullion, and coins of gold, silver, platinum, palladium, copper, and any other metal for the company's own account and the account of

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<sup>5</sup> A bank-ineligible security is any security that a state member bank is not permitted to underwrite or deal in under 12 U.S.C. §§ 24 and 335.

<sup>6</sup> This reference does not include acting as a dealer in options based on indices of bank-ineligible securities when the options are traded on securities exchanges. These options are securities for purposes of the federal securities laws and bank-ineligible securities for purposes of Section 20 of the Glass-Steagall Act, 12 U.S.C. § 337. Similarly, this reference does not include acting as a dealer in any other instrument that is a bank-ineligible security for purposes of Section 20. Bank holding companies that deal in these instruments must do so in accordance with the Federal Reserve's orders on dealing in bank-ineligible securities.

others, and providing incidental services such as arranging for storage, safe custody, assaying, and shipment.

14. Management consulting and counseling activities.

(i) Management consulting.

(A) Providing management consulting advice:<sup>7</sup>

- (1) On any matter to unaffiliated depository institutions, including commercial banks, savings and loan associations, savings banks, credit unions, industrial banks, Morris Plan banks, cooperative banks, industrial loan companies, trust companies, and branches or agencies of foreign banks;
- (2) On any financial, economic, accounting, or audit matter to any other company.

(B) Revenues derived from, or assets related to, a company's management consulting activities under this subparagraph will not be considered to be financial if the company:

- (1) Owns or controls, directly or indirectly, more than 5% of the voting securities of the client institution; or
- (2) Allows a management official, as defined in 12 C.F.R. § 212.2(h), of the company or any of its affiliates to serve as a management official of the client institution, except where such interlocking relationship is permitted pursuant to an exemption permitted by the Federal Reserve.

(C) Up to 30% of a nonbank company's assets or revenues related to management consulting services provided to customers not described in paragraph (A)(1) or regarding matters not described in paragraph (A)(2) above will be included in the company's financial assets or revenues.

(ii) Employee benefits consulting services. Providing consulting services to employee benefit, compensation and insurance plans, including designing plans, assisting in the implementation of plans, providing administrative

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<sup>7</sup> In performing this activity, companies are not authorized to perform tasks or operations or provide services to client institutions either on a daily or continuing basis, except as necessary to instruct the client institution on how to perform such services for itself. See also the Federal Reserve's interpretation of bank management consulting advice (12 C.F.R. § 225.131).

services to plans, and developing employee communication programs for plans.

- (iii) Career counseling services. Providing career counseling services to:
  - (A) A financial organization<sup>8</sup> and individuals currently employed by, or recently displaced from, a financial organization;
  - (B) Individuals who are seeking employment at a financial organization; and
  - (C) Individuals who are currently employed in or who seek positions in the finance, accounting, and audit departments of any company.

15. Support services.

- (i) Courier services. Providing courier services for:
  - (A) Checks, commercial papers, documents, and written instruments (excluding currency or bearer-type negotiable instruments) that are exchanged among banks and financial institutions; and
  - (B) Audit and accounting media of a banking or financial nature and other business records and documents used in processing such media.<sup>9</sup>
- (ii) Printing and selling MICR-encoded items. Printing and selling checks and related documents, including corporate image checks, cash tickets, voucher checks, deposit slips, savings withdrawal packages, and other forms that require Magnetic Ink Character Recognition (MICR) encoding.

16. Insurance agency and underwriting.

- (i) Credit insurance. Acting as principal, agent, or broker for insurance (including home mortgage redemption insurance) that is:
  - (A) Directly related to an extension of credit by the company or any of its subsidiaries; and

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<sup>8</sup> Financial organization refers to insured depository institution holding companies and their subsidiaries, other than nonbanking affiliates of diversified savings and loan holding companies that engage in activities not permissible under Section 4(c)(8) of the BHC Act (12 U.S.C. § 1842(c)(8)).

<sup>9</sup> See also the Federal Reserve's interpretation on courier activities (12 C.F.R. § 225.129), which sets forth conditions for company entry into the activity.

- (B) Limited to ensuring the repayment of the outstanding balance due on the extension of credit<sup>10</sup> in the event of the death, disability, or involuntary unemployment of the debtor.
- (ii) Finance company subsidiary. Acting as agent or broker for insurance directly related to an extension of credit by a finance company<sup>11</sup> that is a subsidiary of a company, if:
  - (A) The insurance is limited to ensuring repayment of the outstanding balance on such extension of credit in the event of loss or damage to any property used as collateral for the extension of credit; and
  - (B) The extension of credit is not more than \$10,000, or \$25,000 if it is to finance the purchase of a residential manufactured home<sup>12</sup> and the credit is secured by the home; and
  - (C) The applicant commits to notify borrowers in writing that:
    - (1) They are not required to purchase such insurance from the applicant;
    - (2) Such insurance does not insure any interest of the borrower in the collateral; and
    - (3) The applicant will accept more comprehensive property insurance in place of such single-interest insurance.
- (iii) Insurance in small towns. Engaging in any insurance agency activity in a place where the company or a subsidiary has a lending office and that:
  - (A) Has a population not exceeding 5,000 (as shown in the preceding decennial census); or

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<sup>10</sup> Extension of credit includes direct loans to borrowers, loans purchased from other lenders, and leases of real or personal property so long as the leases are nonoperating and full-payout leases that meet the requirements of paragraph (8) (Leasing personal or real property) of this annex.

<sup>11</sup> Finance company includes all non-deposit-taking financial institutions that engage in a significant degree of consumer lending (excluding lending secured by first mortgages) and all financial institutions specifically defined by individual states as finance companies and that engage in a significant degree of consumer lending.

<sup>12</sup> These limitations increase at the end of each calendar year, beginning with 1982, by the percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers published by the Bureau of Labor Statistics.



- (B) Has inadequate insurance agency facilities, as determined by the Federal Reserve, after notice and opportunity for hearing.
- (iv) Insurance-agency activities conducted on May 1, 1982. Engaging in any specific insurance-agency activity<sup>13</sup> if the company, or subsidiary conducting the specific activity, conducted such activity on May 1, 1982, or received Federal Reserve approval to conduct such activity on or before May 1, 1982.<sup>14</sup> Revenues derived from, or assets related to, a company's specific insurance agency activity under this clause will be considered financial only if the company:
  - (A) Engages in such specific insurance agency activity only at locations:
    - (1) In the state in which the company has its principal place of business (as defined in 12 U.S.C. § 1842(d));
    - (2) In any state or states immediately adjacent to such state; and
    - (3) In any state in which the specific insurance-agency activity was conducted (or was approved to be conducted) by such company or subsidiary thereof or by any other subsidiary of such company on May 1, 1982; and
  - (B) Provides other insurance coverages that may become available after May 1, 1982, so long as those coverages insure against the types of risks as (or are otherwise functionally equivalent to) coverages sold or approved to be sold on May 1, 1982, by the company or subsidiary.
- (v) Supervision of retail insurance agents. Supervising on behalf of insurance underwriters the activities of retail insurance agents who sell:
  - (A) Fidelity insurance and property and casualty insurance on the real and personal property used in the operations of the company or its subsidiaries; and

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<sup>13</sup> Nothing contained in this provision precludes a subsidiary that is authorized to engage in a specific insurance-agency activity under this clause from continuing to engage in the particular activity after merger with an affiliate, if the merger is for legitimate business purposes.

<sup>14</sup> For the purposes of this paragraph, activities engaged in on May 1, 1982, include activities carried on subsequently as the result of an application to engage in such activities pending before the Federal Reserve on May 1, 1982, and approved subsequently by the Federal Reserve or as the result of the acquisition by such company pursuant to a binding written contract entered into on or before May 1, 1982, of another company engaged in such activities at the time of the acquisition.

- (B) Group insurance that protects the employees of the company or its subsidiaries.
- (vi) Small companies. Engaging in any insurance-agency activity if the company has total consolidated assets of \$50 million or less. Revenues derived from, or assets related to, a company's insurance-agency activities under this paragraph will be considered financial only if the company does not engage in the sale of life insurance or annuities except as provided in paragraphs 15(i) (Credit insurance) and 15(ii) (Finance company subsidiary) above, and does not continue to engage in insurance-agency activities pursuant to this provision more than 90 days after the end of the quarterly reporting period in which total assets of the company and its subsidiaries exceed \$50 million.
- (vii) Insurance-agency activities conducted before 1971. Engaging in any insurance-agency activity performed at any location in the United States directly or indirectly by a company that was engaged in insurance-agency activities prior to January 1, 1971, as a consequence of approval by the Federal Reserve prior to January 1, 1971.

17. Community development activities.

- (i) Financing and investment activities. Making equity and debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas by providing housing, services, or jobs for residents.
- (ii) Advisory activities. Providing advisory and related services for programs designed primarily to promote community welfare.

18. Money orders, savings bonds, and traveler's checks. The issuance and sale at retail of money orders and similar consumer-type payment instruments; the sale of U.S. savings bonds; and the issuance and sale of traveler's checks.

19. Data processing.

- (i) Providing data processing, data storage and data transmission services, facilities (including data processing, data storage and data transmission hardware, software, documentation, or operating personnel), databases, advice, and access to such services, facilities, or data-bases by any technological means, if the data to be processed, stored or furnished are financial, banking or economic.
- (ii) Up to 30% of a nonbank company's assets or revenues related to providing general purpose hardware in connection with providing data processing products or services described in the immediately preceding paragraph will be included in the company's financial assets or revenues.

20. Providing administrative and other services to mutual funds.
21. Owning shares of a securities exchange.
22. Certification authority. Acting as a certification authority for digital signatures and authenticating the identity of persons conducting financial and nonfinancial transactions.
23. Employment histories. Providing employment histories to third parties for use in making credit decisions and to depository institutions and their affiliates for use in the ordinary course of business.
24. Check cashing and wire transmission. Check cashing and wire transmission services.
25. Services offered in connection with banking services. In connection with offering banking services, providing notary public services, selling postage stamps and postage-paid envelopes, providing vehicle registration services, and selling public transportation tickets and tokens.
26. Real estate title abstracting.
27. Providing management consulting services, including to any person with respect to nonfinancial matters, so long as the management consulting services are advisory and do not allow the company to control the person to which the services are provided.
28. Operating a travel agency in connection with financial services.
29. Organizing, sponsoring, and managing a mutual fund.
30. Commercial banking and other banking activities.
31. Directly, or indirectly acquiring or controlling, whether as principal, on behalf of 1 or more entities, or otherwise, shares, assets, or ownership interests (including debt or equity securities, partnership interests, trust certificates, or other instruments representing ownership) of a company or other entity, whether or not constituting control of such company or entity, engaged in any activity not financial in nature as defined in this annex if:
  - (i) Such shares, assets, or ownership interests are acquired and held as part of a bona fide underwriting or merchant or investment banking activity, including investment activities engaged in for the purpose of appreciation and ultimate resale or disposition of the investment;
  - (ii) Such shares, assets, or ownership interests are held for a period of time to enable the sale or disposition thereof on a reasonable basis consistent with the

financial viability of the activities described in the immediately preceding paragraph; and

- (iii) During the period such shares, assets, or ownership interests are held, the company does not routinely manage or operate such company or entity except as may be necessary or required to obtain a reasonable return on investment upon resale or disposition.
32. Directly or indirectly acquiring or controlling, whether as principal, on behalf of 1 or more entities, or otherwise, shares, assets, or ownership interests (including debt or equity securities, partnership interests, trust certificates or other instruments representing ownership) of a company or other entity, whether or not constituting control of such company or entity, engaged in any activity not financial in nature as defined in this annex if:
- (i) Such shares, assets, or ownership interests are acquired and held by an insurance company that is predominantly engaged in underwriting life, accident and health, or property and casualty insurance (other than credit-related insurance) or providing and issuing annuities;
  - (ii) Such shares, assets, or ownership interests represent an investment made in the ordinary course of business of such insurance company in accordance with relevant state law governing such investments; and
  - (iii) During the period such shares, assets, or ownership interests are held, the company does not routinely manage or operate such company except as may be necessary or required to obtain a reasonable return on investment.
33. Lending, exchanging, transferring, investing for others, or safeguarding financial assets other than money or securities.
34. Providing any device or other instrumentality for transferring money or other financial assets.
35. Arranging, effecting, or facilitating financial transactions for the account of third parties.

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