Interexchange Services. (CC Docket No. 96–21).

Filed By: Frank W. Krogh and Donald J. Elardo, Attorneys for MCI Telecommunications Corporation on 08/08/96.

Federal Communications Commission.

William F. Caton,

Acting Secretary.

[FR Doc. 96–23676 Filed 9–16–96; 8:45 am]

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FEDERAL RESERVE SYSTEM

[Docket No. R–0932]

10 Percent Revenue Limit on Bank-Ineligible Activities of Subsidiaries of Bank Holding Companies Engaged in Underwriting and Dealing in Securities

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Notice.

SUMMARY: The Board is adopting a change in the manner in which interest earned on certain securities held by a company in an underwriting or dealing capacity is treated in determining whether the company is engaged principally in underwriting and dealing in securities for purposes of section 20 of the Glass-Steagall Act. In order to ensure compliance with section 20, the Board requires that the revenue a company derives from underwriting and dealing in securities that a member bank may not underwrite or deal in (ineligible securities) not exceed 10 percent of the total revenue of the company. The Board is amending its section 20 orders to specify that interest earned on the types of debt securities that a member bank may hold for its own account is not to be treated as revenue from underwriting or dealing in securities for purposes of section 20. Interest on these securities will continue to be included in total revenue. Section 20 subsidiaries may use this method to compute compliance with the revenue limitation in reports filed with the Board after the effective date of this amendment.

EFFECTIVE DATE: November 12, 1996.

FOR FURTHER INFORMATION CONTACT: Gregory A. Baer, Managing Senior Counsel (202/452–3236), Thomas M. Corsi, Senior Attorney (202/452–3275), Legal Division; Michael J. Schoenfeld, Senior Securities Regulation Analyst (202/452–2781), Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve System. For the hearing impaired *only*, Telecommunication Device for the Deaf, Dorthea Thompson (202/452–3544), Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW, Washington, D.C.

SUPPLEMENTARY INFORMATION:

Background

Beginning with orders issued in 1987, the Board has authorized certain nonbank subsidiaries of bank holding companies, so-called section 20 subsidiaries, to underwrite and deal in ineligible securities.[1] In order to ensure compliance with section 20 of the Glass-Steagall Act, the Board provided that the gross revenue derived by a section 20 subsidiary from underwriting and dealing in ineligible securities not exceed 10 percent of the total gross revenue of the subsidiary, when revenue is averaged over a rolling 8-quarter period.[2]

For purposes of complying with the 10 percent revenue limit, section 20 subsidiaries have reported all interest they earn on third-party ineligible debt securities held in an underwriting or dealing capacity as revenue derived from underwriting and dealing in ineligible securities.[3] Questions have been raised as to whether this treatment is appropriate for interest earned on debt securities that a member bank is authorized to hold for its own account under the Glass-Steagall Act. Accordingly, on July 31, 1996, the Board sought public comment on a proposal to amend its section 20 orders to provide that interest earned by a section 20 subsidiary on the types of debt securities that a member bank may hold would no longer be treated as ineligible revenue.[4]

Summary of Public Comments

The Board received a total of 38 public comments in response to its proposal. All but two of the commenters expressed support for the Board's proposal for the reasons noted in the Board's request for public comments.

One commenter noted that the Board's request for comment on the proposal did not address either the effect the proposal would have on section 20 subsidiaries, or the possibility that the proposal could permit section 20 subsidiaries to manipulate the revenue limitation.[5] This commenter suggested that the Board defer action on the proposal until it examined these issues and included the result of that examination in a second notice requesting public comment on the proposal. More generally, the commenter stated that comprehensive reform and modernization of the financial services industry by Congress is the only means by which banks and securities firms will be able to compete and affiliate on a fair and rational basis. For this reason, the commenter urged the Board to defer action on this and other proposed amendments to its section 20 orders.

Several commenters urged the Board to clarify or expand its proposal. Five commenters opined that the Board should allow section 20 subsidiaries to treat income derived from holding *any* security (as opposed to only those securities a member bank may hold) as eligible revenue—that is, toward total revenue but not ineligible revenue. Four commenters also asserted that section 20 subsidiaries should be able to treat the profit earned from trading in securities for investment purposes, as opposed to dealing in securities, as eligible revenue, particularly with respect to securities that member banks may invest in.

Discussion

After reviewing the public comments, and for the reasons set forth below, the Board has decided to adopt the proposed amendment without change. The Board believes that it is not appropriate to treat interest earned on securities that a member bank is expressly authorized by the Glass-Steagall Act to hold as revenue from underwriting and dealing in ineligible securities.[6] Banks hold such securities for their own account, and buy and sell them on a relatively frequent basis as part of managing their investment portfolio. In recognition of this activity, the Financial Accounting Standards Board changed its accounting rules at the end of 1993 to establish separate accounting treatment for bank portfolio securities that are ''available for sale''

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[1] *E.g., Citicorp*, 73 Federal Reserve Bulletin 473 (1987), *aff'd, Securities Industry Association* v. *Board of Governors*, 839 F.2d 47 (2d Cir.), *cert. denied*, 486 U.S. 1059 (1988).

[2] Section 20 provides that a member bank may not be affiliated with a company that is ''engaged principally'' in underwriting and dealing in securities. 12 U.S.C. 377. Section 20 does not prohibit a bank affiliate from underwriting and dealing in securities that banks may underwrite and deal in directly (eligible securities).

[3] Instructions for Preparation of the Financial Statements for a Bank Holding Company Subsidiary Engaged in Bank-Ineligible Securities Underwriting and Dealing, Form FR Y–20. Schedule SUD-I, Line Item 5 (December 1994)(FR Y–20 Instructions); *see also* ''Structuring Bank-Eligible and Bank-Ineligible Transactions'' in FR Y–20 Instructions.

[4] 61 FR 40642 (1996).

[5] The other commenter who urged the Board not to adopt this proposal did not set forth any reasons for opposing it.

[6] 12 U.S.C. 24 (Seventh), 335; 12 CFR 1.3.

and not intended to be held to maturity.[7]

Furthermore, the Board believes that there is a distinction between the interest earned by a section 20 subsidiary from holding these kinds of securities and the profit made from underwriting or reselling them. The profit or loss a section 20 subsidiary earns on the resale of ineligible debt securities the subsidiary holds in inventory is the revenue that should be attributed to performing the functions of dealing in or underwriting these securities, the critical element of which is the actual offering and sale of the instruments involved.[8] On the other hand, the interest a subsidiary earns on ineligible debt securities while it holds them in inventory is revenue best attributed to holding the securities as a member bank may do under the Glass-Steagall Act.[9]

Accordingly, the Board is amending its section 20 orders to specify that a section 20 subsidiary may treat interest earned on the types of debt securities that a member bank may hold for its own account, either for investment or as an underwriter or dealer, as eligible revenue in calculating compliance with the Board's revenue limitation.

With respect to the suggestion to defer action on this proposal, the Board does not believe that the impact of this interpretation on any particular firm is relevant to whether the interpretation properly reflects the requirements of section 20. However, the Board has used proprietary data to consider the impact the proposal could be expected to have on each section 20 subsidiary based on its activities and portfolio composition during prior quarters. Review of reports and other data provided by the section 20 subsidiaries indicates that the impact of the change will vary considerably depending on the products offered and inventory maintained by each subsidiary, as well as the profitability of those products.[10]

Similarly, the Board does not believe that there would be any benefit in seeking additional public comment regarding manipulation of the revenue test that could arise from the proposed amendment. The Board does not believe that the amendment would lead to manipulation of the test. Interest earned on a security is sufficiently distinct from the profit earned or loss incurred on a security as to allow the Board to monitor the appropriate classification of revenue. As noted, the Board's quarterly report for section 20 subsidiaries requires that they report interest income and dividends received separately from profit or loss.

Furthermore, the Board has supervised revenue test compliance by section 20 subsidiaries for nine years, and has developed substantial experience in ensuring that section 20 subsidiaries properly classify a variety of different types of revenue in computing compliance with the limitation on ineligible revenue.[11] Section 20 subsidiaries have adopted policies, procedures, accounting systems, and related controls to ensure proper classification of revenues. The Board expects section 20 subsidiaries will amend accounting systems and controls as necessary, and that internal auditors will continue to monitor revenue test compliance and revise their audit programs in response to the Board's action.

The Board will review suggestions for further changes offered by commenters at a later date.

By order of the Board of Governors of the Federal Reserve System, September 11, 1996.[12]

William W. Wiles,

Secretary of the Board.

[FR Doc. 96–23728 Filed 9–16–96; 8:45 am]

BILLING CODE 6210–01–P

[7] Statement of Financial Accounting Standards No. 115.

[8] For purposes of the section 20 revenue limitation, the Board has viewed ''public sale'' to include the activity of dealing in securities—the process of buying and reselling to the public specific securities as part of an ongoing, regular business. *E.g., Citicorp, supra,* at 506–08. The term ''underwriting'' generally refers to the process by which new issues of securities are offered and sold to the public. *E.g., Securities Industry Association* v. *Board of Governors,* 807 F.2d 1052, 1062–66 (D.C. Cir. 1986), *cert. denied,* 483 U.S. 1005 (1987).

[9] This distinction is further reflected in the current reporting requirements for section 20 subsidiaries and in Generally Accepted Accounting Principles for bank holding companies, which prescribe that interest revenue be reported separately from gains or losses on securities owned. FR Y–20 Instructions, Statement of Income, Schedule SUD-I, Line Items 2, 5); Securities and Exchange Commission FOCUS Report (Form X–17A–5 Part II) and instructions thereto. Generally Accepted Accounting Principles incorporate the format of the FOCUS Report.

[10] The change will have the greatest impact on those section 20 subsidiaries with debt and equity underwriting powers who are primary dealers and maintain substantial inventories of government and investment-grade ineligible debt securities. Data for two recent quarters indicates that if the change had been in effect, quarterly ineligible revenue for each such company would have decreased between 19 percent and 79 percent.

[11] As noted above, section 20 subsidiaries currently report interest income and dividends received separately from profit or loss on Form FR Y–20.

[12] Voting for this action: Chairman Greenspan, Vice Chair Rivlin, and Governors Kelley, Lindsey, Phillips, Yellen and Meyer.

Change in Bank Control Notices; Acquisitions of Shares of Banks or Bank Holding Companies

The notificants listed below have applied under the Change in Bank Control Act (12 U.S.C. 1817(j)) and § 225.41 of the Board's Regulation Y (12 CFR 225.41) to acquire a bank or bank holding company. The factors that are considered in acting on the notices are set forth in paragraph 7 of the Act (12 U.S.C. 1817(j)(7)).

The notices are available for immediate inspection at the Federal Reserve Bank indicated. Once the notices have been accepted for processing, they will also be available for inspection at the offices of the Board of Governors. Interested persons may express their views in writing to the Reserve Bank indicated for that notice or to the offices of the Board of Governors. Comments must be received not later than September 23, 1996.

A. Federal Reserve Bank of Kansas City (John E. Yorke, Senior Vice President) 925 Grand Avenue, Kansas City, Missouri 64198:

1. Jon and Angela Pope, both of Hoxie, Kansas; to acquire an additional 29 percent, for a total of 52 percent, and Lois Madison, Hoxie, Kansas, to acquire an additional 9 percent, for a total of 30 percent, of the voting shares of Northwest Bancshares, Inc. Rexford, Kansas, and thereby indirectly acquire Peoples State Bank, Colby, Kansas.

Board of Governors of the Federal Reserve System, September 9, 1996.

Jennifer J. Johnson,

Deputy Secretary of the Board.

[FR Doc. 96–23483 Filed 9-16-96; 8:45 am]

BILLING CODE 6210-01-F

Change in Bank Control Notices; Acquisitions of Shares of Banks or Bank Holding Companies

The notificants listed below have applied under the Change in Bank Control Act (12 U.S.C. 1817(j)) and § 225.41 of the Board's Regulation Y (12 CFR 225.41) to acquire a bank or bank holding company. The factors that are considered in acting on the notices are set forth in paragraph 7 of the Act (12 U.S.C. 1817(j)(7)).

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