

FEDERAL RESERVE press release



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For immediate release

June 30, 1999

The Federal Reserve Board today announced its approval of the notice filed by BankBoston Corporation, Boston, Massachusetts; The Bank of New York Company, Inc., New York, New York; The Chase Manhattan Corporation, New York, New York; Citizens Financial Group, Inc., Providence, Rhode Island; Comerica Incorporated, Detroit, Michigan; First Union Corporation, Charlotte, North Carolina; Fleet Financial Group, Inc., Boston, Massachusetts; HSBC Holdings PLC, London, England; HSBC Holdings BV, Amsterdam, The Netherlands; HSBC Americas, Inc., Buffalo, New York; The Royal Bank of Scotland Group PLC, Edinburgh, Scotland; The Royal Bank of Scotland PLC, Edinburgh, Scotland; and Summit Bancorp, Princeton, New Jersey, to acquire Magic Line, Inc., Dearborn, Michigan, through NYCE Corporation, Woodcliff Lake, New Jersey, and thereby engage in providing data processing services and check verification services.

Attached is the Board's Order relating to this action.

Attachment

FEDERAL RESERVE SYSTEM

BankBoston Corporation
Boston, Massachusetts

The Bank of New York Company, Inc.
New York, New York

The Chase Manhattan Corporation
New York, New York

Citizens Financial Group, Inc.
Providence, Rhode Island

Comerica Incorporated
Detroit, Michigan

First Union Corporation
Charlotte, North Carolina

Fleet Financial Group, Inc.
Boston, Massachusetts

HSBC Holdings PLC
London, England

HSBC Holdings BV
Amsterdam, The Netherlands

HSBC Americas, Inc.
Buffalo, New York

The Royal Bank of Scotland Group PLC
Edinburgh, Scotland

The Royal Bank of Scotland PLC
Edinburgh, Scotland
Summit Bancorp
Princeton, New Jersey

Order Approving Notice to Conduct Certain Data Processing Activities
and Other Nonbanking Activities

BankBoston Corporation, a bank holding company within the meaning of the Bank Holding Company Act (“BHC Act”), and the other bank holding companies listed in the Appendix to this order (collectively, “Notificants”), have requested the Board’s approval under section 4(c)(8) of the BHC Act (12 U.S.C. § 1843(c)(8)) and section 225.24 of the Board’s Regulation Y (12 C.F.R. 225.24) to acquire Magic Line, Inc., Dearborn, Michigan (“Magic Line”), through NYCE Corporation, Woodcliff Lake, New Jersey (“NYCE”), and thereby engage in providing data processing services in accordance with section 225.28(b)(14) of Regulation Y (12 C.F.R. 225.28(b)(14)).¹ In addition, Notificants, through NYCE, would engage in providing check verification services, in accordance with section 225.28(b)(2) of Regulation Y (12 C.F.R. 225.28(b)(2)).

NYCE operates an electronic funds transfer (“EFT”) network under the NYCE service name, and Magic Line operates the Magic Line EFT network. Both NYCE and Magic Line provide data processing and transmission services to financial institutions and merchants that are members of their respective branded automated teller machine (“ATM”) and point of sale (“POS”) networks.² NYCE

¹ Notificants, with the exception of Comerica Incorporated (“Comerica”), are shareholders of NYCE and would each retain 5 percent or more of the voting shares of NYCE. Comerica is a principal shareholder of Magic Line and would acquire more than 5 percent of the voting shares of NYCE as a result of the proposed transaction. This notice also includes Comerica’s request for the Board’s approval to acquire, through NYCE, an interest in Card Alert Services, Inc., Arlington, Virginia, and thereby engage in providing debit card fraud detection services.

² In general, an ATM network is an arrangement whereby more than one ATM and more than one depository institution (or the depository records of such

(continued...)

would engage directly and through Magic Line in certain nonbanking activities related to the operation of ATM and POS networks, including various data processing and transmission services.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (64 Federal Register 13,799 (1999)). The time for filing comments has expired, and the Board has considered the notice and all comments received in light of the factors set forth in section 4(c)(8) of the BHC Act.

Notificants are commercial banking organizations with headquarters in Massachusetts, Michigan, New Jersey, New York, North Carolina, and Rhode Island, and foreign banking organizations with subsidiary commercial banking organizations in the United States. Each Notificant engages directly and through subsidiaries in a broad range of banking and permissible nonbanking activities in the United States and abroad.³

Section 4(c)(8) of the BHC Act provides that a bank holding company may, with Board approval, engage in any activity that the Board determines to be “so closely related to banking or managing or controlling banks as to be a proper

²(...continued)

institutions) are connected by electronic or telecommunications means to one or more computers, processors, or switches for the purpose of providing automated teller services to retail customers of the depository institutions. POS terminals accept ATM or similar cards from retail customers and, using an ATM network or a parallel POS-only network, provide access to a retail customer’s account to transfer funds to a merchant’s account. POS terminals are generally located in merchant establishments.

³ Asset and deposit data for each Notificant are set forth in the Appendix.

incident thereto.”⁴ The Board previously has determined that providing check verification services and EFT-related data processing and transmission services is closely related to banking within the meaning of section 4(c)(8) of the BHC Act.⁵ Notificants would conduct the proposed activities in accordance with Regulation Y and previous Board decisions.⁶

In determining whether activities proposed to be conducted in a specific proposal are a “proper incident” to banking or managing or controlling banks, the Board must determine whether the performance of the proposed activities by Notificants through Magic Line “can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices.”⁷ The Board has received comments opposing the proposal from two EFT networks (“Protestants”) that generally allege that consummation of the proposal would result in significant anti-competitive effects in the market for EFT services in Michigan, Indiana, and Illinois outside the Chicago Metropolitan Statistical Area (“Upper Midwest”). In particular, Protestants argue that a

⁴ 12 U.S.C. § 1843(c)(8).

⁵ See 12 C.F.R. 225.28(b)(2) and (14); Barnett Banks of Florida, Inc., 65 Federal Reserve Bulletin 263 (1979) (check verification services); Compagnie Financière de Paribas, 82 Federal Reserve Bulletin 348 (1996) (fraud detection services); Bank of New York Company, Inc., 80 Federal Reserve Bulletin 1107 (1994) (“InfiNet Order”) (ATM network services); Banc One Corporation, 81 Federal Reserve Bulletin 492 (1995) (“EPS Order”) (ATM network services).

⁶ The Board notes that ATM activities must be conducted in accordance with applicable federal and state laws, including applicable branching laws.

⁷ See 12 U.S.C. § 1843(c)(8).

requirement under the proposal that certain Magic Line shareholders use NYCE as their exclusive regional network in the Upper Midwest for three years after consummation of the proposal is intended primarily to prevent Protestants and other EFT networks from competing with NYCE in this area.

The Board has carefully considered these comments in light of all the facts of record, including written submissions by Notificants and Protestants. As in similar cases, the Board also sought comments from the Department of Justice on the competitive effects of the proposal. The Department of Justice indicated that it had no objection to consummation of the proposal.

Competitive Considerations

In order to determine whether a particular transaction is likely to decrease competition, the Board has considered the area of effective competition between parties. The area of effective competition has been defined by reference to the line of commerce, or product market, and a geographic market. The Board has carefully considered the relevant product and geographic markets in which to analyze the competitive effects of the proposal in light of all the facts of record, including information provided by Notificants and Protestants and the geographic scope of and services provided by existing EFT networks and other providers of EFT services.

The Board previously has identified three distinct products that are typically offered by EFT networks:

- (1) Network access (access to an EFT network identified by a common trademark or logo displayed on ATMs, POS terminals, and access cards);
- (2) Network services (operation of a “network switch” to receive and route electronic messages between ATMs, POS terminals, and data processing facilities used by depository institutions to authorize EFT

transactions and the provision of “gateway” access to other EFT networks); and

- (3) ATM/POS processing (data processing and transmission services used to drive ATMs and POS terminals, monitor their activity, authorize EFT transactions, and reconcile accounts).⁸

Both NYCE and Magic Line provide all three services to their network members and these three activities define the areas in which NYCE and Magic Line compete. Accordingly, the relevant product markets in which to examine the competitive effects of the proposal are the markets for network access, network services, and ATM/POS processing.

The Board previously has determined that the geographic market for network access is an area significantly larger than local banking markets and consists of a region comprising several states.⁹ Based on all the facts of record, the Board believes that NYCE has a significant competitive presence in the New England and northeastern states (Connecticut, Delaware, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont). Magic Line’s primary service area is in the central United States (Indiana, Illinois, Kentucky, Michigan, and Ohio). Thus, the primary service areas for network access services of NYCE and Magic Line do not overlap.

NYCE and Magic Line compete in providing network access services to a limited extent in several states. There are a number of considerations, however, that mitigate any decrease in existing or potential competition resulting from the proposal. Changes in concentration in the market for network access services in

⁸ See EPS Order at 493-94.

⁹ See EPS Order at 494.

these states would not be significant.¹⁰ Moreover, in each state, a number of other networks, including other large regional networks, and third party processors would continue to operate and to provide both direct and potential competition for NYCE. Smaller networks and third party processors also would continue to operate EFT networks within the central United States and to provide both direct and potential competition for the Magic Line network.¹¹ Finally, national networks increasingly offer an alternative to regional networks for some financial institutions in the central United States.¹²

The Board considers the appropriate geographic market area for evaluating the provision of network services and ATM/POS processing services to be national in scope. The Board notes that physical proximity to ATMs and POS terminals is not required to provide these services and that these services may be provided on an unbranded or subcontract basis. In addition, large scale economies can be achieved in these product markets, and several firms offer ATM/POS processing services on a national basis. Many smaller firms also offer

¹⁰ NYCE and Magic Line both operate branded ATMs in 15 states. In 13 of these states, the smaller of the two networks provides branded access to less than 2 percent of the estimated total number of ATMs in the state. In Illinois, where NYCE is the smaller network, it provides branded access to less than 3 percent of the estimated total number of ATMs in the state. In Kentucky, NYCE provides branded access to less than 5 percent of the estimated total number of ATMs, and its brand would appear on approximately 16 percent of such ATMs after consummation of the proposal.

¹¹ The Board also notes the rapid growth in recent years in the volume of POS transactions, which serve as an alternative for certain ATM transactions, and the presence of a number of competitors that provide POS network services across regional boundaries.

¹² See HONOR/Most Order at 133 n.20. For example, in October 1998, Visa began operations of its Visa II card, a debit card for POS transactions.

these services. Based on all the facts of record, the Board finds that the proposal would not have a significantly adverse effect on competition in the provision of these services in the central United States or any other relevant portion of the country.

Protestants claim, however, that a proposed agreement (“Shareholder Agreement”) between NYCE and certain Magic Line shareholders would constitute a form of unfair competition or would decrease competition to the extent that the Shareholder Agreement prevents these shareholders from joining Protestants or other regional networks in the Upper Midwest.¹³ Protestants further assert that the terms of the Shareholder Agreement are contrary to the terms of EFT operating rules that the Board has specifically relied on in previous cases to support its

¹³ Under the Shareholder Agreement, any Magic Line shareholder that receives cash or EFT transaction processing credits as any portion of the consideration for its Magic Line shares must use NYCE as its exclusive regional EFT network in the Upper Midwest for three years after consummation of the proposal, and must make specific minimum annual payments to NYCE for data processing and related services during these three years based on a percentage of the shareholder’s ATM transaction volume prior to the proposal. In addition, a party to the Shareholder Agreement must purchase from NYCE for the term of the agreement any data processing services that are of the kind it obtained from Magic Line at the time that NYCE and Magic Line agreed to merge. A Magic Line shareholder may elect at any time during the term of the Shareholder Agreement to terminate its exclusive network routing requirement, but as a consequence the term of the agreement for purchasing data processing services would be extended to five years and the shareholder’s minimum annual payment obligation would be increased.

Protestants contend that the focus of the Shareholder Agreement on certain geographic areas and certain EFT-related services demonstrates that the purpose of the Shareholder Agreement is to harm Protestants rather than to facilitate the transfer of the Magic Line franchise.

determination in those cases that the combination of two EFT networks would not have a significantly adverse effect on competition.¹⁴

The Board has reviewed the Shareholder Agreement in light of all the facts of record in this case. In the Michigan portion of the Upper Midwest, where Magic Line is a dominant EFT network, the Shareholder Agreement would apply to three Magic Line shareholders.¹⁵ These shareholders operate approximately 17 percent of the estimated total number of ATMs in the state and account for approximately 27 percent of the estimated total number of ATM transactions in the state. Accordingly, approximately three-fourths of all ATM transactions in Michigan would be unencumbered by the Shareholder Agreement and would be immediately available to competing networks.

Two of the three Magic Line shareholders in Michigan that would be subject to the Shareholder Agreement have experienced substantial growth in their EFT transaction volume and data processing fees.¹⁶ This growth, if sustained, would enable these shareholders to shift a substantial portion of their EFT activities to a regional network other than NYCE with limited concern that they would be financially penalized by the minimum annual payment requirement of the Shareholder Agreement for doing so.

¹⁴ See BankAmerica Corporation, 85 Federal Reserve Bulletin 271 (1999); HONOR/Most Order at 133; EPS Order at 496; InfiNet Order at 1109.

¹⁵ In the other two states in the Upper Midwest, Illinois and Indiana, Magic Line shareholders are estimated to operate only 5 percent and 2 percent, respectively, of the total number of ATMs in the state. Accordingly, the Shareholder Agreement would not appear to have a significant effect on competition among EFT networks and third party processors in these areas.

¹⁶ These two shareholders control more than 90 percent of all the ATMs controlled by the three shareholders in the aggregate in Michigan.

Moreover, these provisions of the Shareholder Agreement are limited in duration. The exclusivity provision is applicable to each of these shareholders for three years.¹⁷

The Board is concerned that exclusivity provisions, such as those in the Shareholder Agreement, are inherently anti-competitive because they restrict the ability of some participating financial institutions to choose ATM network access and ATM service providers that may be less costly and more suitable for customers of these financial institutions. In this case, the Board believes that the potential adverse effects of the Shareholder Agreement are real, but recognizes that the anti-competitive effects of the Shareholder Agreement are limited in geographic area, scope, and duration.

Other Considerations

¹⁷ The Board also has considered the Shareholder Agreement in comparison to covenants not to compete. The Board and the courts have previously determined that such covenants are permissible when they are reasonable in duration, scope, and geographic area. See Orbanco, Inc., 59 Federal Reserve Bulletin 367 (1973); United Jersey Banks, 69 Federal Reserve Bulletin 565, 567 n.12 (1983); Business Records Corporation v. Lueth, 981 F.2d 957 (9th Cir. 1992) (“Lueth”). Such covenants have been upheld by the courts when they are made in connection with the sale of a business because such covenants facilitate the transferability of property, in the form of the goodwill of a business. See Lueth at 960; Ticor Title Insurance Company v. Cohen, 173 F.2d 63 (2d Cir. 1999). Accordingly, in sale of business cases, the duration of a covenant not to compete has been upheld when it is reasonably related to the time required to vest the goodwill of a business in its new owner. See Lueth at 961; Restatement (Second) of Contracts § 188, comments (d) and (f) (American Law Institute 1981). This period of time must be determined in light of all the relevant circumstances. See Laidlaw, Inc. v. Student Transportation of America, Inc., 20 F. Supp.2d 727 (D.N.J. 1998). The Board believes that the exclusivity provisions of the Shareholder Agreement are consistent with the court decisions regarding covenants not to compete.

In considering the proper incident test, the Board also must determine whether the likely public benefits of a proposal could reasonably be expected to outweigh potential adverse effects. Notificants assert that the proposal would result in significant public benefits.

As part of the proposal, NYCE has committed to adopt unified operating rules for NYCE and Magic Line that, in several important respects, would facilitate competition and increase access to the network for all depository institutions. The NYCE unified operating rules would allow all depository institutions in the combined networks to join other regional and national networks. The operating rules also would allow all depository institutions to designate networks other than NYCE as the priority routing for transactions performed by the depository institution's customers (subject to the other networks granting reciprocal rights to their participants to use NYCE). In addition, participants would be able to co-brand access cards and ATMs and to use third party processors and branded subswitching of transactions.¹⁸ Moreover, depository institutions of all sizes would be able to participate in NYCE on a nondiscriminatory basis. By contrast, the current Magic Line operating rules contain several provisions concerning transaction routing, co-branding of access cards, and ATM processing services that tend to restrict competition with other regional EFT networks and with third party processors.

Consummation of the proposal, therefore, would facilitate competition throughout the Magic Line service area in the provision of network access, network

¹⁸ "Subswitching" refers to the routing of transactions between members of the same regional network without accessing that network, and, therefore, without paying the network's switch fee. Typically, this is accomplished by routing the transaction through a third party processor that provided ATM processing services for both network members.

services, and ATM/POS processing. The unified NYCE operating rules would promote competition among NYCE and alternative providers of EFT-related services, including other regional networks, national networks, and third party processors, that is currently limited or foreclosed under the Magic Line operating rules. The proposal also would ensure access to the network by all depository institutions and competition among them in providing network access to their customers.

The combination of NYCE and Magic Line upon consummation of the proposal also would benefit consumers by providing greater account availability and convenience to customers of each network. In particular, an ATM network that has a large number of financial institution members and that provides network access at more locations over a broad geographical area would have greater value to network cardholders and provide broader and more convenient access to customer accounts. Smaller financial institutions that compete with larger, multistate organizations for deposit funds would be able to expand their depositors' access to their accounts without making substantial investments in branch systems or proprietary ATM networks.

Consummation of the proposal also would result in other public benefits. The proposal is expected to produce economies of scale, for example, and to reduce average costs for the combined networks. Members of each network also would benefit from the technical expertise and the expanded research and development programs of the combined network. Notificants anticipate that the increased capital base of NYCE would enable it to develop and market new products and services more rapidly, thereby increasing competition among EFT networks and third party processors.

As part of this review under section 4(c)(8) of the BHC Act, the Board also considers the financial and managerial resources of Notificants and their subsidiaries and any company to be acquired, and the effect of the proposal on those resources.¹⁹ Based on all the facts of record, including reports of examination and other supervisory information, the Board concludes that financial and managerial considerations are consistent with approval of the proposal. In addition, there is no evidence in the record that the proposal would result in conflicts of interests or unsound banking practices.

As explained above, aspects of this proposal are likely to result in some decrease in competition while other aspects of the proposal promote competition and have other public benefits. The Board is particularly concerned about the serious potential anti-competitive effects that may arise from the exclusivity provisions of the Shareholder Agreement used by Notificants. As a general matter, the Board believes that the likely effect on competition from exclusivity provisions of the type contained in the Shareholder Agreement would outweigh the typical public benefits associated with the increased convenience and economies of scale associated with a merger of ATM networks. In this case, however, the Board believes that the potential adverse effect on competition is somewhat mitigated by the limited application, duration, and scope of the Shareholder Agreement. Importantly, the Board also believes that significant public benefits in the form of increased and more open competition are likely to result from the commitment by NYCE to change the Magic Line operating rules to allow all depository institutions in the network to join other regional and national networks, to facilitate increased use of third party processors, to route transactions more freely through other networks, and to co-brand access cards and ATMs. Absent the

¹⁹ See 12 C.F.R. 225.26.

unique facts in this case concerning the actual operation of the Shareholder Agreement, and the commitment of NYCE to adopt unified operating rules as described above, the expected public benefits in this case would likely not be sufficient to outweigh the possible adverse effects. On this basis and after careful consideration of all the facts of record, the Board has determined that consummation of the proposal can reasonably be expected to produce public benefits that would outweigh any possible adverse effects under the proper incident to banking standard of section 4(c)(8) of the BHC Act.

Conclusion

Based on all the facts of record, the Board has determined that the notice should be, and hereby is, approved. The Board's approval is specifically conditioned on Notificants' compliance with the commitments made in connection with this notice and the conditions referred to in this order. The Board's determination also is subject to all the terms and conditions set forth in Regulation Y, including those in sections 225.7 and 225.25(c) (12 C.F.R. 225.7 and 225.25(c)), and to the Board's authority to require modification or termination of the activities of a bank holding company or any of its subsidiaries that the Board finds necessary to ensure compliance with, or to prevent evasion of, the provisions and purposes of the BHC Act and the Board's regulations and orders issued thereunder. For purposes of this action, the commitments and conditions shall be deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

This proposal shall not be consummated later than three months after the effective date of this order, unless such period is extended for good cause by the Board, or the Federal Reserve Banks of Boston, Chicago, New York, or Richmond, acting pursuant to delegated authority.

By order of the Board of Governors,²⁰ effective June 28, 1999.

(signed)

Robert deV. Frierson
Associate Secretary of the Board

²⁰ Voting for this action: Chairman Greenspan, Vice Chair Rivlin, and Governors Kelley, Meyer, Ferguson, and Gramlich.

APPENDIX

Asset and Deposit Data for Notificants²¹

BankBoston Corporation, with approximately \$52.6 billion in total consolidated assets, is the 15th largest commercial banking organization in the United States, controlling \$35 billion in deposits. BankBoston Corporation operates subsidiary banks in six states.

The Bank of New York Company, Inc., with approximately \$46.7 billion in total consolidated assets, is the 17th largest commercial banking organization in the United States, controlling \$27.5 billion in deposits. The Bank of New York Company, Inc., operates subsidiary banks in six states.

The Chase Manhattan Corporation, with approximately \$246.9 billion in total consolidated assets, is the 2d largest commercial banking organization in the United States, controlling \$133.5 billion in deposits. The Chase Manhattan Corporation operates subsidiary banks in seven states, the Commonwealth of Puerto Rico, and the U.S. Virgin Islands.

HSBC Holdings PLC and HSBC Holdings BV, with approximately \$471 billion in total consolidated assets, are the fifth largest commercial banking organization in the world, controlling \$333 billion in deposits. Through their subsidiary, HSBC Americas, Inc., with approximately \$31.8 billion in total consolidated assets, they are the 28th largest commercial banking organization in the United States, controlling \$21.6 billion in deposits. HSBC Americas, Inc., operates a subsidiary bank in one state.

Comerica Incorporated, with approximately \$36.6 billion in total consolidated assets, is the 23d largest commercial banking organization in the United States, controlling \$23.3 billion in deposits. Comerica Incorporated operates subsidiary banks in four states.

First Union Corporation, with approximately \$212.1 billion in total consolidated assets, is the fourth largest commercial banking organization in the United States,

²¹ U.S. asset data are as of December 31, 1998, and U.S. deposit data are as of June 30, 1998. Worldwide asset and deposit data are as of December 31, 1997.

controlling \$138.2 billion in deposits. First Union Corporation operates subsidiary banks in 12 states and the District of Columbia.

Fleet Financial Group, Inc., with approximately \$114.8 billion in total consolidated assets, is the seventh largest commercial banking organization in the United States, controlling \$69.3 billion in deposits. Fleet Financial Group, Inc., operates subsidiary banks in eight states.

Royal Bank of Scotland Group PLC and Royal Bank of Scotland, with approximately \$117 billion in total consolidated assets, are the 67th largest commercial banking organization in the world, controlling \$85 billion in deposits. Through their subsidiary, Citizens Financial Group, Inc., with approximately \$6 billion in total consolidated assets, they are the 81st largest commercial banking organization in the United States, controlling \$4.9 billion in deposits. Citizens Financial Group, Inc., operates subsidiary banks in two states.

Summit Bancorp, with approximately \$32.4 billion in total consolidated assets, is the 27th largest commercial banking organization in the United States, controlling \$22.7 billion in deposits. Summit Bancorp operates a subsidiary bank in two states.