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Statement by

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Mr. Chairman, Members of the Committee, it is a pleasure to testify in support of the International Banking Act of 1977. This landmark legislation is very important to American consumers and businesses, to Federal and State bank regulatory authorities and legislators, to the management of monetary policy, and to U.S. relations with our trading partners. Without attempting to weigh the importance of each relative interest, because all must be considered fairly, I would emphasize that the bill is a domestic bank regulatory measure and should be so characterized. The only unique thing about foreign bank offices in this country is that they are owned and managed from abroad mostly by large multinational banks with worldwide assets exceeding one billion dollars. As these hearings will indicate, they are also a very large and rapidly growing part of our domestic banking system. Their banking services are sold to American consumers and businesses and they compete directly with domestic banks that are regulated and supervised under a comprehensive system of Federal and State laws and regulations.

I am optimistic that these hearings will lead to the enactment of a law that is fair and appropriate for all parties, embodying the principle of national treatment for foreign banks and conforming their regulation evenly and equitably to that imposed on similar domestic banking organizations. My optimism is based on these facts. Last year this Committee did an outstanding job in proposing an International Banking Act to the full House which passed as H.R. 13876. The appropriate Subcommittee of the Senate held a full set of hearings on this proposal and was prevented from continuing this work only because of the adjournment

of the Congress. Further, proposals of this kind have been before the Congress and the public since 1974, and there has been ample opportunity for the Congress to hear all points of view germane to this bill.

Two things have happened in this process. First, the original legislative proposals have been changed significantly to meet some basic objections, and the Federal Reserve has recommended further changes which, in our judgment, should meet the remaining points of controversy. Second, those who foresaw a continued and rapid growth of foreign bank operations in the United States have seen their predictions fulfilled. Since the introduction of the Board's first proposal in 1974, foreign bank operations in this country have continued to grow in number, size, and importance. They have been assuming an increasingly important share of the market for commercial and industrial loans, have been increasing their penetration into regional markets and retail banking services, and have been active participants in domestic money markets. Our most recent data show that 210 banking facilities are operated by 94 foreign banks in the United States. More than half of these foreign banks operate across State lines: twenty-two foreign banks have banking offices in three or more States and another twenty-eight foreign banks have banking offices in two States, an advantage denied to domestic banks. Foreign bank interest in the United States is growing at a remarkably rapid pace and even the most partisan of those who oppose any form of Federal regulation must grant that further delay will surely complicate the work of the Congress in enacting appropriate legislation.

Mr. Chairman, I am submitting with my testimony a Statistical Appendix providing data on the growth of foreign bank operations and

a compendium of supporting documents intended for the Committee's use. In today's statement, I would like to address those provisions of the Act that may be questioned by later witnesses.

As recently as three years ago, many held the belief that foreign banks in our economy were highly specialized institutions operating only in port and gateway cities where international trade was important, and those opposed to legislation argued that their chartering and regulation could be left to the States. Such arguments today, in view of the extraordinary expansion of these banks in the context of the development of multinational banking, have been thoroughly disproved.

The rapid expansion of multinational banking has been occurring abroad as well as in the United States. The growth of this international financial community is testing the regulatory frameworks and monetary system in many other countries. In Belgium, the Netherlands, the United Kingdom and Canada, banking laws are currently being revised. Other countries are reviewing their existing regulations and supervisory practices. The business this Committee is about is thus very common in other nations and it is an entirely responsible and appropriate activity. For the United States is alone among the leading trading nations of the western world, in having virtually no national policy, monetary controls, or national presence where foreign banks are concerned.

Over the past several years, as we have testified before, we have generally found the banking authorities in other countries to be sympathetic and understanding of the need to rationalize the treatment

of foreign banks in our country with our domestic banking system. Many foreign central bankers consider it surprising that the United States does not have a national policy on foreign banks, and, in particular, they recognize the logic of extending monetary and credit controls to foreign banks operating within our borders, and conducting transactions in our currency. This, of course, is a fundamental reason for enacting this bill.

The Committee should not be misled by criticism from commercial bankers abroad. The objections to the legislation addressed to those sections of the bill that would require divestitures or the closing of existing facilities can be dealt with during the legislative process. Objections to the United States having appropriate powers to guide monetary and credit policies within this country should not be given undue weight.

In the Board's letter to you endorsing the present legislation, there are included proposals for amendments addressed to the most valid concerns of those opposing certain of its sections. I would like to touch on these amendatory proposals and underline their importance to the success of the legislation before you.

I have referred to monetary policy controls, and your bill largely accomplishes the objective of establishing for foreign banks a fair equivalent to the monetary regulations that affect comparable domestic banking institutions. The bill does not require formal membership in the Federal Reserve System. It simply requires that those

foreign banks operating in the United States that have $1 billion or more in worldwide bank assets maintain reserves in the same way as the largest U.S. banks, virtually all of which are members of the Federal Reserve System.

There is, however, an omission in the present bill. The State-chartered subsidiaries of large foreign banks are exempted from monetary controls. The Board believes that the appropriate test for the imposition of monetary controls is the size and the ability of a foreign bank to compete and participate through its U.S. affiliates in our large money and credit markets. Thus, the Board recommends that Section 7 of the bill be amended to require that Federal Reserve monetary controls be applied to all the U.S. operations of a foreign bank that has $1 billion or more in worldwide bank assets, irrespective of whether they are conducted through agencies, branches, subsidiary banks, or subsidiary New York Investment Companies. If we omit one corporate form of organization from such restrictions, the bill's purpose will be subverted and its effectiveness severely reduced.

Consistent with national treatment, section 5 of the bill generally subjects foreign banks to the same multi-State restrictions that apply to domestic banks. The Board believes, however, that direct imposition of the branching restrictions of the McFadden Act should be limited to Federal branches and agencies. State branches should be put on the same competitive footing as State banks in their home State. In this way, foreign banks may benefit from future reciprocal interstate branching legislation that may be agreed upon among the States.

In our previous comments on the bill, we suggested that multi-State restrictions apply to both branches and agencies of foreign banks. I expect you will hear strong testimony from State authorities urging that agencies remain exempted from multi-State branching restrictions as the bill now provides. The Board has carefully considered these arguments which arise quite naturally from those States interested in attracting offices of foreign banks to assist in expanding their local industries' participation in foreign trade. I would like now to propose what appears to be a reasonable alternative. That alternative would be to limit agencies of foreign banks that are licensed by the States in the future to powers that are no greater than Federally-chartered Edge Act Corporations. These future State-licensed agencies would thus be able to conduct a full service international banking business and thus promote the further development of international trade and investment throughout the country. At the same time, the multi-State restrictions on banking offices conducting a full service domestic banking business would not be compromised. To exempt agencies entirely would, in our judgment, exacerbate the present multi-State advantages enjoyed by foreign banks, as, traditionally, agencies have been the most important form of foreign bank activity. This alternative would equitably meet the interests of the States that wish to have international banking agencies, the interests of foreign banks that wish to establish international banking facilities in more than one trade center and the public interest of competitive equality with our domestic banks.

The issue of deposit insurance on foreign bank operations in order to protect U.S. consumers and businesses has been debated since 1974. Following the action of this Committee and the House vote on H.R. 13876 last year, the Federal Deposit Insurance Corporation suggested in comments to the Senate a method of applying deposit insurance to the domestic deposits of U.S. branches of foreign banks. In the judgment of the Board, that alternative is far more desirable than the present Section 6 of the bill. The Board favors compulsory FDIC insurance on deposits in branches of foreign banks. The arguments for extending FDIC insurance to these deposits are very direct and simple. The United States has enjoyed an extraordinarily successful system of deposit insurance protecting in its end effect jobs, businesses and our economies locally, regionally and nationally since the 1930's. It is a model act covering virtually all full-service commercial banks in this country. It is being studied and copied by foreign governments. It would be a curious turn of events to abandon our world leadership in this area by substituting an imperfect form of protection. Surety bonds or pledges of assets cannot be considered comparable to the certainty of FDIC insurance and the Federal Deposit Insurance Corporation's ability to protect our citizens from bank failures.

Because of the continuing rapid growth of foreign bank operations in this country, it will become progressively more difficult to adopt grandfathering proposals for their existing activities that are equitable and consistent with prior legislative precedent. Your bill grandfathers

multi-State banking operations as of May 1, 1976. Nonbanking activities, other than securities affiliates, are permanently grandfathered as of December 3, 1974. The Board concurs strongly in the permanent grandfathering of these activities and believes it appropriate for the Congress to review the existing grandfathering dates. A majority of the Board believes these dates should be brought forward to afford equitable treatment to all existing facilities.

As for securities affiliates, it will be recalled that the Senate hearings on the International Banking Act of 1976 produced extensive controversy concerning the securities affiliate provisions in the present bill. The Board urges that the securities affiliations that are in place today be permanently grandfathered to quiet the controversy, and that, as a safeguard, the Board be given the discretion to review these activities under the nonbanking standards of the Bank Holding Company Act for any abuses that might arise over time. This would meet the concerns expressed by the regional stock exchanges. It would also provide some certainty to foreign banks that their securities affiliates, which are still a very small part of the securities industry, could continue to operate in essentially the same form and relative size as at present.

As we have indicated to the Committee, the Board does not see the necessity for the detailed guideline provisions on foreign bank entry in Section 9 of the bill. The State and Federal regulatory agencies already have appropriate statutory requirements that must be fulfilled by those who apply for permission to conduct a banking business in this

country. The provisions of the bill, which provide for consultation between bank regulatory authorities and the Secretaries of State and Treasury on new foreign bank applications, would seem entirely adequate to insure that any important foreign policy issues are considered when appropriate. I would expect that in almost all cases this consultative procedure would be entirely routine.

Legitimate issues that have been raised by foreign banks concerning fair national treatment include a key issue related to the nonbanking prohibitions of the Bank Holding Company Act. Last year there apparently was a misconception on the part of some foreign bankers, who thought that the nonbanking prohibitions that we apply to banks in our domestic market would seriously interfere with their nonbanking interests abroad. For that reason we have proposed a clarifying amendment to this bill whereby foreign banks that are principally engaged in banking abroad would not be prohibited from retaining or acquiring interests in foreign-chartered, nonbanking companies that have U.S. activities, but which are principally engaged in business outside the United States. While the Board believes it has sufficient regulatory authority under present law to deal with such problems, we also believe it would be desirable for the Congress to embody this principle in the statute. In this proposal, we have included a requirement that any banking transactions with U.S. offices of such foreign affiliates be conducted at competitive rates and terms. In this way the firm or bank involved would not have an unfair advantage over their respective U.S. competitors.

The Board's carefully considered and strong support of the International Banking Act of 1977 is based on the conviction that the proposed bill with the amendments that we have recommended would fairly implement the principle of national treatment of foreign banking organizations operating in the United States. In the opinion of the Board, as we have repeatedly emphasized, that principle is the only workable and equitable method of dealing with these organizations.

As I have suggested in this testimony, most responsible objections to the legislation have been or can be met. The question then is simply: should we not put foreign and domestic banks on a relatively equal footing now, for surely they should be in time. This legislation is an essential ingredient in the larger process of rationalizing and modernizing our own banking laws. That work will be fairer and easier if it is evenly applicable to all banks as it would be under this legislation.

The conscientious and excellent work of Congress and the Committee should continue until this bill is passed. The Federal Reserve is ready to assist in any way necessary.

Thank you.