FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 68-1
January 2, 1968

**To all Banks, Nonbank Financial
Institutions and Other Firms Addressed
in the Eleventh Federal Reserve District:**

There is enclosed a copy of amended guidelines for the 1968 Voluntary Foreign Credit Restraint Program applicable to commercial banks and nonbank financial institutions. These guidelines, which are effective as of January 1, 1968, replace those issued by this Bank on November 17, 1967, Circular No. 67-227. Quoted below is the text of the press release issued by the Board of Governors covering these new guidelines:

"The Board of Governors of the Federal Reserve System today issued revised guidelines, effective immediately, for restraint of foreign credits by banks and other financial institutions.

"The revised guidelines, which are substantially more restrictive than those issued on November 16, 1967, are a part of the President's program announced today, to strengthen the U.S. balance of payments. The new guidelines are designed to achieve a net inflow of at least $500 million during 1968.

"Ceilings on foreign credit extensions by banks were revised as follows:

"For banks whose ceilings had been set at 109 per cent of their 1964 base (i.e., the amount of foreign credits they had outstanding on December 31, 1964), the new ceiling for 1968 will now be 103 per cent. For other, smaller banks whose ceilings had been set at 2 per cent of their total assets on December 31, 1966, the new ceilings for 1968 will now be an amount equal to their 1967 ceiling plus one-third of the addition to that ceiling envisaged in the original 1968 guidelines.

"The banks also are asked to reduce outstanding term loans to developed countries of continental Western Europe (i.e., loans with maturities of one year or more) by not renewing such loans at maturity, and by not relending the repayments of such loans to residents of those countries. The guidelines request that short-term loans to developed countries of continental Western Europe be reduced during 1968 by 40 per cent of the amount outstanding on December 31, 1967, at a rate of not less than 10 percentage points in each quarter.

"Revised guidelines for nonbank financial institutions request that holdings of foreign assets covered by the program be reduced during 1968 by 5 per cent or more compared to the amount of such assets held on December 31, 1967. It is expected that holdings of liquid funds abroad (deposits and money market instruments) will be reduced to zero, or to the minimum working balance required to conduct foreign business activities, even if this entails a decline in foreign assets by more than 5 per cent. The nonbank financial institutions, which include insurance companies, trust companies, mutual savings banks, etc., are requested to refrain from making any new loans or investments in developed countries of continental Western Europe other than those judged essential for the financing of U.S. exports.

"The Board pointed out that the guidelines have been designed to focus the major effect of the reduction on the developed countries of continental Western Europe without adverse effects on credits necessary to finance U.S. exports or on credits to developing countries.

"In issuing the revised guidelines the Board expressed its confidence that the financial community fully appreciates the urgency of improving the balance of payments and that the splendid cooperation exhibited by participants in the credit restraint program thus far will continue, despite the heavier burden now imposed."

Additional copies of these guidelines may be obtained from this Bank or appropriate branch. Questions concerning this program should be directed to Assistant Vice President Cowan.

Yours very truly,

Watrous H. Irons
President

Enclosure

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Effective
January 1, 1968

PREFACE TO GUIDELINES

1968

The President of the United States has acted to strengthen the country's balance of payments. An integral part of the President's program is a substantial tightening of restraint on foreign lending by financial institutions. Accordingly, the Board of Governors has revised the guidelines for banks and other financial institutions as follows:

The Revised 1968 Program for Commercial Banks

The 1968 ceiling for banks accounting for about 95 per cent of the 1967 ceiling will be 103 per cent of the end-1964 base. Banks whose target ceiling for 1967 was less than 2 per cent of total assets as of December 31, 1966, may take the latter figure as their 1968 ceiling. However, such banks are asked to use not more than one-third of the amount by which this figure exceeds their 1967 ceiling during the course of 1968. These banks are requested not to exceed their 1967 ceiling, even within the limitation set forth above, except to make priority credits, i.e., export credits or credits to developing countries.

All banks are requested to reduce the amount of term loans (loans with original maturities of more than one year) to residents of developed countries of continental Western Europe by not renewing such loans at maturity, and by not relending the repayments of such loans to other residents of those countries. Each bank will reduce its ceiling on each reporting date by the amount of the reduction in term loans to Western Europe during the preceding month.

All banks also are asked to reduce the amount of short-term credit outstanding (loans with maturities of one year or less) to developed countries of continental Western Europe by 40 per cent of the amount of such credit outstanding on December 31, 1967. This reduction is to be achieved at a minimum rate of 10 per cent per quarter, cumulative, and the ceiling will be reduced correspondingly. That is, each bank is asked at the end of each quarter to reduce its ceiling for 1968 by 10 per cent of the amount of short-term credits to developed countries of Western Europe outstanding on December 31, 1967, and to achieve at least an equivalent reduction in such credits during the quarter.

These revisions in the guidelines are designed to induce a net inflow of capital to the financial institutions during 1968. Since the major effects of the revisions are focused on the developed countries of continental Western Europe, it should be possible to achieve this inflow without endangering other important national objectives, such as export promotion and the supplying of capital to the developing countries.

The Revised 1968 Program for Nonbank Financial Institutions

The revised program for 1968 differs from the program announced on November 16, 1967, in the following ways:

1. All institutions are now requested to reduce their holdings of foreign assets covered by this revised program by 5 per cent or

more during 1968, with the target reduction based on the amount of such assets held on December 31, 1967.

2. Institutions generally are expected to reduce their holdings of liquid funds abroad to zero during 1968, except to the extent that minimum working balances are required for the conduct of foreign business activities.

3. Institutions are expected also to refrain from making any new investments, in either debt or equity form, in the developed countries of continental Western Europe, except for new credits judged essential to the financing of U.S. exports as evidenced by exemption from the Interest Equalization Tax that otherwise would apply.

4. The definition of covered assets is changed: (a) to exclude foreign assets of types otherwise covered by the program but acquired as "free delivery" items after December 31, 1967; and (b) to provide that covered equity securities held at the beginning of 1968 be carried throughout 1968 at the values reflected in the report (on Form FR 392R-68) filed for December 31, 1967, and that covered equities purchased during 1968 be carried at cost.

The revised program is unchanged from the 1968 program announced earlier, in the following ways:

1. Among the types of foreign assets covered by the program, institutions are still requested to give absolute priority to credits that represent financing essential to the sale of U.S. goods abroad.

2. Institutions may continue to invest in non-covered foreign assets as desired.

3. Only financial institutions holding covered assets of $500,000 or more, or total foreign assets of $5 million or more, are asked to file quarterly reports with their Federal Reserve Bank. However, institutions with holdings below these amounts are also expected to abide by the provisions of the program.

4. The group of institutions covered by the nonbank guidelines continues to include trust companies and trust departments of commercial banks, mutual savings banks, insurance companies, investment companies, finance companies, employee retirement and pension funds, college endowment funds, and charitable foundations. Also included are the U.S. branches of foreign insurance companies and of other foreign nonbank financial corporations. Investment underwriting firms, securities brokers and dealers, and investment counseling firms also are covered with respect to foreign financial assets held for their own account and are requested to inform their customers of the program in those cases where it appears applicable.

GUIDELINES FOR BANKS

1. Ceiling and Reporting

A. Meaning of terms

(1) "Foreigners" include individuals, partnerships, and corporations domiciled outside the United States, irrespective of citizenship, except their agencies or branches located within the United States; branches, subsidiaries, and affiliates of U.S. banks and other U.S. corporations that are located in foreign countries; and any government of a foreign country or official agency thereof and any official international or regional institution created by treaty, irrespective of location.

(2) "Foreign long-term securities" are those issued without a contractual maturity or with an original maturity of more than 1 year from the date of issuance.

(3) "Other claims" include all long-term claims other than securities, real assets, net investment in and advances to foreign branches and subsidiaries, and all short-term claims (such as deposits, money market instruments, customers' liability on acceptances, and loans).

(4) "Nonexport credit" means a foreign credit other than one that arises directly out of the financing of exports of U.S. goods or services or that is reasonably necessary for the financing of such exports.

(5) "Developed countries" are Abu Dhabi, Australia, Austria, the Bahamas, Bahrain, Belgium, Bermuda, Canada, Denmark, France, Germany (Federal Republic), Hong Kong, Iran, Iraq, Ireland, Italy, Japan, Kuwait, Kuwait-Saudi Arabia Neutral Zone, Libya, Liechtenstein, Luxembourg, Monaco, Netherlands, New Zealand, Norway, Portugal, Qatar, Republic of South Africa, San Marino, Saudi Arabia, Spain, Sweden, Switzerland, and the United Kingdom. Also to be considered "developed" are the following countries: Albania, Bulgaria, any part of China that is dominated or controlled by international communism, Cuba, Czechoslovakia, Estonia, Hungary, any part of Korea that is dominated or controlled by international communism, Latvia, Lithuania, Outer Mongolia, Poland (including any area under its provisional administration), Rumania, Soviet Zone of Germany and the Soviet sector of Berlin, Tibet, Union of Soviet Socialist Republics and the Kurile Islands, Southern Sakhalin, and areas in East Prussia that are under the provisional administration of the Union of Soviet Socialist Republics, and any part of Vietnam that is dominated or controlled by international communism.

B. Specific inclusions and exclusions in calculating the ceiling

(1) Claims on foreigners should be included without deduction of any offsets. Foreign long-term securities held for banks' own account should be included. Foreign customers' liability for acceptances executed should be included whether or not the acceptances are held by the reporting bank. Participations purchased in loans to foreigners (except loans guaranteed or participated in by the Export-Import Bank or insured by the Foreign Credit Insurance Association) should be included;

also, foreign assets sold to U.S. residents, including the Export-Import Bank, with recourse should be included.

(2) Contingent claims, unutilized credits, claims held for account of customers, acceptances executed by other U.S. banks and loans guaranteed or participated in by the Export-Import Bank or insured by the Foreign Credit Insurance Association, should be excluded.

C. Ceiling

(1) Foreign credits included in the ceiling are a bank's total claims on foreigners held for own account, with the specific inclusions and exclusions set forth in Section B above. The 1968 ceiling for a bank reporting on Form F.R. 391 on October 31, 1967, and that had foreign assets of $500,000 or more on that date is either: (1) 103 per cent of the amount of foreign assets held on December 31, 1964, or (2) an amount equal to (a) its 1967 ceiling under the guidelines issued in December 1966 plus (b) one-third of the difference between that amount and 2 per cent of the bank's total assets as of December 31, 1966, whichever is larger.

(2) All banks are requested, effective from the date of the announcement of these revised guidelines, to refrain from renewing term loans (those with original maturities of more than one year) to residents of developed countries of continental Western Europe, or relending amounts received in repayment of such loans, except to make bona fide export credits. The ceiling of each bank receiving such repayments will be adjusted monthly by deducting therefrom the dollar amount of those repayments.

(3) All banks are requested further to reduce the amount of outstanding short-term credits (credits with original maturities of one year or less) to residents of developed countries of continental Western Europe by 40 per cent of the amount of such credits held on December 31, 1967, during the course of 1968. This reduction should be made at a rate of at least 10 percentage points in each quarter; the ceiling for each bank will be reduced correspondingly, i.e., quarterly by an amount equal to 10 per cent of the amount outstanding on December 31, 1967.

(4) Any bank that sells a foreign asset to a U.S. resident, including the Export-Import Bank, without recourse should reduce its ceiling by an equivalent amount.

(5) A bank that had no ceiling in 1967, or that had foreign assets of $500,000 or less on October 31, 1967, may discuss with the Federal Reserve Bank of the Federal Reserve district in which it is located, the possibility of adopting a special ceiling adequate to permit the bank to meet reasonable priority credit demands of existing customers or originating in its normal trade area.

In discussing the ceiling of such a bank, the Federal Reserve Bank will ascertain the bank's previous history in foreign transactions, including acceptance of foreign deposits or handling foreign collections, and the reasons why the bank considers that it should engage in foreign transactions.

D. Reporting

(1) Banks that report on Treasury Foreign Exchange Forms B-2 or B-3, or that have been granted special ceilings under provisions of these guidelines, should file a Monthly Report on Foreign Claims (Form F.R. 391/68R) with the Federal Reserve Bank of the Federal Reserve district in which the bank is located.

(2) Copies of Form F.R. 391/68R are available at the Federal Reserve Banks.

2. Loans Guaranteed by the Export-Import Bank

Loans guaranteed or participated in by the Export-Import Bank or insured by the Foreign Credit Insurance Association are excluded from the ceiling. The role of the Export-Import Bank within the framework of the President's program is coordinated by the National Advisory Council for International Monetary and Financial Policies.

3. Credits in Excess of Ceiling

A bank would not be considered as acting in a manner inconsistent with the program if it temporarily exceeds its ceiling as a result of the extension of bona fide export credits.

The bank should, however, refrain from making new extensions of non-priority credits so as to reduce its claims on foreigners to an amount within the ceiling as quickly as possible. It should also take every opportunity to withdraw or reduce commitments, including credit lines, that are not of a firm nature and to assure that drawings under credit lines are kept to normal levels and usage. At time of renewal, each credit line should be reviewed for consistency with the program.

A bank whose foreign credits are in excess of the ceiling will be invited periodically to discuss with the appropriate Federal Reserve Bank the steps it has taken and proposes to take to reduce its credits to a level within the ceiling.

4. Loan Priorities

Within the ceiling, absolute priority should be given to bona fide export credits. Credits that substitute for cash sales or for sales customarily financed out of nonbank or foreign funds are not entitled to priority.

With respect to nonexport credits, banks should give the highest priority to loans to developing countries and should avoid restrictive policies that would place an undue burden on Canada, Japan, and the United Kingdom.

A bank adopting a 1968 ceiling equal to 2 per cent of its total assets on December 31, 1966, will be expected to restrict the use of any excess over its 1967 ceiling to priority credits (i.e., export credits and credits to developing countries) originating among the bank's regular customers or residents of its trade territory. That is, subject to the limitations set forth in Guideline 1C(1), holdings of foreign credits on any reporting date should not exceed the 1967 ceiling by more than the increase in holdings of priority credits between October 31, 1967, and the reporting date.

5. Trust Departments

Trust departments of commercial banks should follow the guidelines with respect to nonbank financial institutions.

6. Transactions for the Account of Customers

A bank should bear in mind the President's balance of payments program when acting for the account of a customer. Although the bank is obliged to follow a customer's instructions, it should to the extent possible discourage customers from placing liquid funds outside the United States. A bank should not place with a customer foreign obligations that, in the absence of the voluntary credit restraint program, it would have acquired or held for its own account.

7. Foreign Branches

The voluntary credit restraint program is not designed to restrict the extension of foreign credits by foreign branches if the funds utilized are derived from foreign sources and do not add to the outflow of capital from the United States.

Total claims of a bank's domestic offices on its foreign branches (including permanent capital invested in as well as balances due from such branches) represent bank credit to nonresidents for the purposes of the program.

8. "Edge Act" Corporations

"Edge Act" and "Agreement" Corporations are included in the voluntary credit restraint program. Foreign loans and investments of such corporations may be combined with those of the parent bank, or a separate ceiling may be adopted for the parent bank and each such subsidiary corporation. If such corporation is owned by a bank holding company, its foreign loans and investments may be combined for purposes of the program with any one or all of the banks in the holding company group.

9. U.S. Branches and Agencies of Foreign Banks

Branches and agencies of foreign banks located in the United States are requested to act in accordance with the spirit of the domestic commercial bank voluntary credit restraint program.

10. Loans to U.S. Residents and Substitution of Domestic Credit for Credit from Foreign Sources

There are a number of situations in which loans to domestic customers, individual as well as corporate, may be detrimental to the President's balance of payments program and hence should be avoided. Examples are:

(A) Loans to U.S. residents--individuals as well as corporations--that will aid the borrower in making new foreign loans or investments inconsistent with the President's program. Banks should avoid making new loans that would directly or indirectly enable borrowers to use funds abroad in a manner inconsistent with the Department of Commerce program or with the guidelines for nonbank financial institutions.

(B) Loans to U.S. subsidiaries and branches of foreign companies that otherwise might have been made by the bank to the foreign parent or other foreign affiliate of the company, or that normally would have been obtained abroad.

11. Management of a Bank's Liquid Funds

A bank should not place its own funds abroad for short-term investment purposes, whether such investments are payable in foreign currencies or in U.S. dollars. This does not, however, call for a reduction in necessary working balances held with foreign correspondents.

GUIDELINES FOR NONBANK FINANCIAL INSTITUTIONS

Through the end of calendar year 1968, each institution is requested to reduce its aggregate holdings of "covered" foreign financial assets to 95 per cent or less of its "adjusted base-date holdings."

Covered foreign financial assets, subject to the guideline ceiling, include the following types of investments, except for "free delivery" items received after December 31, 1967:

1. Foreign bank deposits, including deposits in foreign branches of U.S. banks, and liquid money market claims on foreign obligors, generally defined to include marketable negotiable instruments maturing in 1 year or less.

2. All other claims on foreign obligors written to mature in 10 years or less at date of acquisition. This category includes all bonds, notes, mortgages, loans, and other credits, regardless of country of origin. Excluded are bonds and notes of international institutions of which the United States is a member, and loans guaranteed or participated in by the Export-Import Bank or insured by the Foreign Credit Insurance Association, regardless of maturity.

3. Net financial investment in foreign branches, financial subsidiaries, and affiliates, located in developed countries other than Canada and Japan.[1] Such financial investment includes payments into equity and other capital accounts of, and net loans and advances to, foreign corporations engaged principally in finance, insurance, or real estate activities, in which the U.S. institution has an ownership interest of 10 per cent or more. Excluded are earnings of a foreign affiliate directly retained in the capital accounts of the foreign corporation.

4. Long-term credits of foreign obligors domiciled in developed countries other than Canada and Japan.[1] Included in this category are bonds, notes, mortgages, loans, and other credits maturing more than 10 years after date of acquisition. Excluded are bonds of international institutions of which the United States is a member.

5. Equity securities of foreign corporations domiciled in developed countries other than Canada and Japan[1] except those acquired after September 30, 1965, in U.S. markets from American investors. The test of whether an equity security is covered will depend on the institution's obligation to pay the Interest Equalization Tax on acquisition. Exclusion from covered assets under this program normally will be indicated when, in acquiring an equity security that otherwise would be covered, the purchasing institution receives a certificate of prior American ownership, or brokerage confirmation thereof.

"Base-date" holdings for any reporting date in 1968 are defined as: (1) total holdings of covered foreign assets as of December 31, 1967; (2) minus, equity securities of companies domiciled in developed countries (except Canada and Japan),[1] that are included in (1) but had been sold to American investors prior to the current quarter; (3) plus, or minus, the difference between sales proceeds and "carrying" value of covered equities sold prior to the current quarter to other than American investors or in other than U.S. markets. On each reporting date in 1968, "carrying" value of covered equities should be the value reflected in the institution's report (on Form FR 392R-68) for December 31, 1967, in the case of equities held on that date, and it should be cost in the case of equities purchased after that date.

"Adjusted" base-date holdings, to which the 95 per cent ceiling applies, are equal to "base-date" holdings as defined above, with the two types of adjustment for sales of included covered equities during the current quarter.

In making foreign loans and investments that are subject to the guideline ceiling, institutions are asked to give absolute priority to credits that represent the bona fide financing of U.S. exports, that is, financing necessary to consummate the export sale. At the same time, institutions generally are expected to reduce their holdings of foreign liquid funds (both deposits and money market instruments) to zero during 1968, even though it entails a reduction in total covered assets considerably larger than 5 per cent. However, an institution may maintain such minimum working balances abroad as are needed for the efficient conduct of its foreign business activities. In addition, institutions are requested to refrain from making any new investments, in either debt or equity form, in the developed countries of continental Western Europe, except for new credits judged essential to the financing of U.S. exports as evidenced by exemption from the Interest Equalization Tax that otherwise would apply.

For some institutions, repatriation of liquid funds, cessation of new investment in the countries of continental Western Europe, and maximum restraint on reinvestment of current maturities of other covered assets may not be sufficient to reduce total covered assets by the target objective of 5 per cent or more. In such instances, or when there are other special circumstances--such as the existence at year-end 1967 of

firm commitments to invest, or the need to accommodate requests for the bona fide financing of U.S. exports--an institution may consult with its Federal Reserve Bank with a view to working out an individually tailored program for achieving an orderly reduction in the institution's covered foreign assets. In the absence of such an arrangement, institutions will be expected to make progress from quarter to quarter on the reduction targeted for the year as a whole.

Foreign financial assets not covered by the guideline are still reportable on the quarterly statistical reports to the Federal Reserve Banks, but are not subject to the target reduction. Such non-covered foreign investments include the following:

1. Bonds and notes of international institutions of which the United States is a member, regardless of maturity.

2. Long-term investments in Canada, Japan, and all developing countries, including credit instruments with final maturities of more than 10 years at date of acquisition, direct investment in financial subsidiaries, and all equity securities issued by firms domiciled in these countries.

3. Equity securities of firms in developed countries other than Canada and Japan that have been acquired in U.S. markets from American investors (see Point 5 above).

Foreign assets of types covered by the program and acquired as "free delivery" items--that is, in new accounts deposited with trust companies or trust departments of commercial banks, or as new gifts received by educational institutions--are not now defined as covered assets, if they are acquired after December 31, 1967. Such assets should be reported as a memorandum item, as should loans guaranteed or participated in by the Export-Import Bank or insured by the Foreign Credit Insurance Association.

Each nonbank financial institution holding, on any quarterly reporting date, covered assets of $500,000 or more, or total foreign financial assets of $5 million or more, is requested to file a statistical report, covering its total holdings on that date, with the Federal Reserve Bank of the Federal Reserve district in which its principal office is located. The reports are due within 20 days following the close of each calendar quarter, and forms may be obtained by contacting the Federal Reserve Bank.

GENERAL CONSIDERATIONS

In cooperating in the voluntary foreign credit restraint program, the nonbank financial institutions are requested to refrain from making loans and investments inconsistent with other aspects of the President's balance of payments program. Among these are the following: (1) non-covered credits under this program that substitute for loans that commercial banks would have made in the absence of that part of the program applicable to them; (2) credits to U.S. corporate borrowers that would enable them to make new foreign loans and investments inconsistent with the corporate part of the program; (3) credits to U.S. subsidiaries and branches of foreign companies that otherwise would have been made to the foreign parent, or that would substitute for funds normally obtained from foreign sources.

The voluntary foreign credit restraint program for nonbank financial institutions does not apply to the investment, within the country involved, of reserves accumulated on insurance policies sold

abroad, in amounts up to 110 per cent of such reserves. Furthermore, in view of the balance of payments objectives of the program, it is noted that covered investments of nonbank financial institutions may be permitted to exceed the guideline ceiling to the extent that the funds for such investment are borrowed in developed countries other than Canada and Japan. Any such arrangements to offset foreign borrowing against foreign investment should be discussed with the Federal Reserve Bank.

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[1] NOTE - Developed countries other than Canada and Japan: continental Western Europe--Austria, Belgium, Denmark, France, Germany (Federal Republic), Italy, Liechtenstein, Luxembourg, Monaco, Netherlands, Norway, Portugal, San Marino, Spain, Sweden, and Switzerland; other developed countries are: Abu Dhabi, Australia, the Bahamas, Bahrain, Bermuda, Hong Kong, Iran, Iraq, Ireland, Kuwait, Kuwait-Saudi Arabia Neutral Zone, Libya, New Zealand, Qatar, Republic of South Africa, Saudi Arabia, and the United Kingdom. Also to be considered "developed" are the following countries: Albania, Bulgaria, any part of China which is dominated or controlled by international communism, Cuba, Czechoslovakia, Estonia, Hungary, any part of Korea which is dominated or controlled by international communism, Latvia, Lithuania, Outer Mongolia, Poland (including any area under its provisional administration), Rumania, Soviet Zone of Germany and the Soviet sector of Berlin, Tibet, Union of Soviet Socialist Republics and the Kurile Islands, Southern Sakhalin, and areas in East Prussia which are under the provisional administration of the Union of Societ Socialist Republics, and any part of Vietnam that is dominated or controlled by international communism.