FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 69-87
April 9, 1969

Revised 1969 Guidelines for Banks and Nonbank Financial Institutions
Under the President's Balance of Payments Program

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

The following statement was made public on April 4, 1969, by the Board of Governors of the Federal Reserve System:

> The Board of Governors of the Federal Reserve System today issued revised 1969 guidelines, effective immediately, covering foreign credits and investments by U. S. banks and other financial institutions. The revisions represent a modification of earlier announced guidelines, and are designed to permit additional flexibility to finance U. S. exports and to resolve some serious equity problems.
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> The Voluntary Foreign Credit Restraint Program (VFCR) is one of several elements in the government's over-all program to strengthen the U. S. balance of payments position.
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> Under the revised guidelines, a bank will either retain its present ceiling on foreign lending or adopt a new ceiling equal to 1½ per cent of its total assets as of December 31, 1968. This formula will permit a modest increase of $400 million in the foreign lending ceilings for banks, which stood at $9.7 billion at the end of last year.
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> For nonbank financial institutions--such as insurance companies, mutual funds, finance companies and bank trust departments--the ceiling on foreign assets will be restored to 100 per cent of the end-of-1967 base. The ceiling had earlier been continued at 95 per cent of that base for the current year. This modification--designed primarily to simplify administration of the program--will increase the ceiling for nonbank financial institutions by an estimated $40 million during 1969. At the end of last year investments by nonbank financial institutions covered by the guidelines amounted to $1.4 billion.
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> Governor Andrew F. Brimmer, who administers the program in behalf of the Board of Governors, said the banks had an unused leeway of $475 million at the end of 1968. Thus the revision would potentially allow banks to increase their existing level of credits to foreigners by about $875 million. It is expected that the full potential will not be used, and a substantial leeway will continue to be maintained. Furthermore, the potential increase will be lessened slightly as bank ceilings continue to be progressively reduced by the amount of repayments of term loans to residents of developed countries of continental Western Europe.

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The program has been in force since February 1965 and was last revised in December of last year when guidelines for 1969 were issued. In considering the program at that time, the Board concluded that the balance of payments prospects for 1969 did not permit any basic change in VFCR. Yet, in view of the need to improve the trade balance, the Board said it planned to re-examine the program early in 1969 to determine whether additional flexibility for financing U. S. exports might be provided in the guidelines.

As part of that review, Governor Brimmer has held a series of seven regional meetings throughout the country at the Federal Reserve Banks of Boston, New York, Philadelphia, Atlanta, Chicago, Dallas, and San Francisco. Representatives of other Federal Reserve Banks and of the reporting commercial banks and other financial institutions participated in these meetings.

Governor Brimmer said it became apparent as the regional meetings progressed that some additional flexibility in the guidelines was needed to finance U. S. exports and to reduce inequities among banks of different size inherent in the VFCR program.

The financing of U. S. exports under the VFCR refers to credits extended by the banks to foreigners to finance purchases from the United States. The program does not affect credits to American producers and exporters to finance U. S. exports.

Under the guidelines issued last December 23, the 1969 ceiling on foreign credit extensions by banks remained at the level specified in the guidelines, as adjusted, of one year earlier. For about one half of the approximately 160 reporting banks (accounting for more than 90 per cent of the aggregate ceiling), this was essentially 103 per cent of the 1964 base. For the remainder of the reporting banks, the ceiling was the 1967 ceiling plus one third of the difference between that amount and 2 per cent of total assets as of December 31, 1966.

The text of the new guidelines is printed on the following pages. If you have questions concerning this program, please contact Vice President Cowan. Additional copies of this circular will be furnished upon request.

Yours very truly,

P. E. Coldwell

President

REVISED GUIDELINES

Banks and Nonbank Financial Institutions

I. GENERAL PURPOSE

In order to help to strengthen the U. S. balance of payments, U. S. financial institutions are asked to continue to restrain their foreign loans and investments.

II. BANKS

A. Ceiling restraints

1. *Basic restraint*

A bank should not hold claims on foreigners (defined in G-2 below) at any time in excess of its ceiling, as determined in 2 below, except for temporary overages as the result of the extension of export credit.

2. *Ceiling*

The foreign lending guideline amount (hereafter "ceiling") for a bank that has been reporting under previous Federal Reserve foreign credit restraint guidelines is the larger of:

a. the ceiling it was expected to observe on December 31, 1968 under the guidelines in existence on that date; or

b. 1½ per cent of its total assets as of December 31, 1968.

3. *Special ceiling*

a. A bank that, on December 31, 1968, had outstanding claims on foreigners of less than $500,000 and that has no special ceiling under previous guidelines may discuss with the Federal Reserve Bank in its District the possibility of adopting a special ceiling adequate to permit the bank to meet reasonable credit demands of existing customers or other reasonable credit demands originating in its normal trade area.

b. In discussing the ceiling of such a bank, the Federal Reserve Bank will take into account the bank's previous experience with foreign transactions, including acceptance of foreign deposits or handling foreign collections, and other circumstances concerning prospects for the bank's engaging in foreign transactions.

4. *Priority credits*

a. Within its ceiling, and as among all types of credit to foreigners, a bank should give first priority to credits to finance exports of U. S. goods (hereafter "export credits") and second priority to credits to developing countries.

b. Export credits that result in sales taking place on credit rather than, in the absence of such credits, on the basis of cash are not to be considered as priority credits.

5. *Western Europe*

a. *Term loans.* Banks should not make new term loans (loans with maturities of over one year) to residents of developed countries of continental Western Europe, except to finance U. S. exports. A bank's ceiling should be reduced each month by the dollar amount of any repayments it receives on term loans to such residents outstanding on December 31, 1967.

b. *Short-term credits.* Banks should hold the amount of short-term credits (credits with original maturities of one year or less) to residents of these countries to not more than 60 per cent of the amounts of such credits outstanding on December 31, 1967.

6. *Equity investments*

Equity investments, including those in developed countries of continental Western Europe, may be made within a bank's ceiling, subject to requirements of the Board of Governors.

7. *Sale of foreign assets*

Any bank that sells a claim on a foreigner that is subject to these restraints, without recourse, (a) to a U. S. resident other than a financial institution participating in the Federal Reserve credit restraint program or other than a direct investor subject to the controls administered by the Department of Commerce or (b) to the Export-Import Bank should reduce its ceiling by an equivalent amount.

8. *Total assets*

For the purpose of calculating a ceiling under A-2-b above, total assets are those shown in the Official Report of Condition, submitted to the relevant supervisory agency, as of December 31, 1968.

B. Exclusions

1. *Canada*

These guidelines are not to restrain the extension of credit to residents of Canada. For the purpose of determining the aggregate amount of a bank's outstanding claims on foreigners, any net increases in claims on residents of Canada after February 29, 1968 should be deducted from total claims on foreign-

ers, and any net reductions in claims on residents of Canada after February 29, 1968 should be added to total claims on foreigners.

2. *Certain guaranteed and insured loans*

Loans to finance U. S. exports that either are guaranteed, or participated in, by the Export-Import Bank, or guaranteed by the Department of Defense, or are insured by the Foreign Credit Insurance Association are exempt from these credit restraints.

C. Temporary overages

1. A bank would not be considered as acting inconsistently with the purpose of the guidelines if it temporarily exceeded its ceiling as the result of the extension of an export credit.

2. Such a bank should, however, refrain from making new extensions of nonpriority 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.

3. 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.

D. Applicability to financial institutions

1. *General*

The guidelines are applicable to all U. S. banks (exclusive of the trust departments of commercial banks, which should follow the guidelines for nonbank financial institutions) and to "Edge Act" and "Agreement" Corporations.

2. *Edge Act and Agreement Corporations*

a. Edge Act or Agreement Corporations that, under previous guidelines, adopted a ceiling separate from those of their parent banks may continue to be guided by a separate ceiling or may combine their foreign loans and investments with those of their parent banks.

b. No special ceilings are provided for Edge Act or Agreement Corporations established after March 3, 1965. An Edge Act or Agreement Corporation which has been established after March 3, 1965, as a subsidiary of one bank should share the ceiling of the respective parent bank. An Edge Act or Agreement Corporation which has been formed after March 3, 1965, and is a subsidiary of two or more banks (not associated in a bank holding company) may be assigned a share or shares of the ceilings of its parent banks. Any contemplated reallocations of ceilings to the Edge Act or Agreement Corporation should be discussed with the Federal Reserve Bank of the District in which the bank desiring to make the transfer is located.

3. *Bank holding companies*

a. A registered bank holding company will be treated as a bank for the purpose of these guidelines.

b. Banks and Edge Act or Agreement Corporations which are owned by a registered bank holding company may consolidate the ceilings of one or more banks in the group.

4. *Foreign branches of U. S. banks*

a. The guidelines are not designed to restrict the extension of foreign credits by foreign branches of U. S. banks if the funds utilized are derived from foreign sources and do not add to the outflow of capital from the United States.

b. 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 foreigners for the purposes of the program.

E. Conformity with objectives of guidelines

1. *Department of Commerce program and nonbank financial institutions guidelines*

Banks should avoid making 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.

2. *Substitute loans*

Banks should not extend to U. S. subsidiaries and to branches of foreign companies loans that otherwise might have been made by the banks to the foreign parent or other affiliate of the company or that normally would have been obtained abroad.

3. *Management of liquid assets*

A bank should not place its own funds abroad (other than in Canada) for short-term investment purposes, whether such investments are payable in foreign currencies or in U. S. dollars. Banks need not, however, reduce necessary working balances held with foreign correspondents.

4. *Transactions for customers*

While recognizing that it must follow a customer's instruction, a bank should discourage cus-

tomers from placing liquid funds outside the United States, except in Canada. A bank should not place with a customer foreign obligations that, in the absence of the guidelines, it would have acquired or held for its own account.

5. *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 these guidelines.

F. Reporting

Each bank that is eligible for a ceiling under these guidelines should file a Monthly Report on Foreign Claims (Form FR 391/69.1) with the Federal Reserve Bank in the District in which the bank is located. (Forms are available at the Federal Reserve Banks.)

G. Definitions

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. "Claims on foreigners" are claims on foreigners held for a bank's own account. They include: foreign long-term securities; foreign customers' liability for acceptances executed, whether or not the acceptances are held by the reporting banks; deferred payment letters of credit described in the Treasury Department's Supplementary Reporting Instruction No. 1, Treasury Foreign Exchange Reports, Banking Forms, dated May 10, 1968; participations purchased in loans to foreigners (except loans guaranteed or participated in by the Export-Import Bank or guaranteed by the Department of Defense, or insured by the Foreign Credit Insurance Association); loans to financial subsidiaries incorporated in the United States, 50 per cent or more of which is owned by foreigners; and foreign assets sold, with recourse, to U. S. residents other than financial institutions participating in the Federal Reserve credit restraint program or direct investors subject to the controls administered by the Commerce Department. "Claims on foreigners" exclude: contingent claims; unutilized credits; claims held for account of customers; acceptances executed by other U. S. banks; loans to finance U. S. exports guaranteed or participated in by the Export-Import Bank or guaranteed by the Department of Defense or insured by the Foreign Credit Insurance Association; and, in the manner determined in B-1 above, claims on residents of Canada.

3. "Credits to finance exports of U. S. goods" and "export credits" are transactions that are identifiable through documents available to the bank.

4. Developing countries are all countries other than: 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; and other than: Albania, Bulgaria, the People's Republic of China, Cuba, Czechoslovakia, Estonia, Hungary, Communist-controlled Korea, 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 Communist-controlled Vietnam.

III. NONBANK FINANCIAL INSTITUTIONS

A. Types of institutions covered

The group of institutions covered by the nonbank guidelines includes: trust companies; trust departments of commercial banks; mutual savings banks; insurance companies; investment companies; finance companies; employee retirement and pension funds; college endowment funds; charitable foundations; and 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. Businesses whose principal activity is the leasing of property and equipment, and which are not owned or controlled by a financial institution, are not defined as financial institutions.

B. Ceiling and priorities

Each institution is requested to limit its aggregate holdings of foreign assets covered by the program to no more than 100 per cent of the adjusted amount of such assets held on December 31, 1967.

Institutions generally are expected to hold no foreign deposits or money market instruments (other than Canadian). However, an institution may maintain such minimum working balances abroad as are needed for the efficient conduct of its foreign business activities.

Among other foreign assets that are subject to the guideline ceiling, institutions are asked to give first priority to credits that represent the bona fide financing of U. S. exports, and second priority to credits to developing countries. In addition, institutions are requested not to increase the total of their investments in the developed countries of continental Western Europe beyond the amount held on December 31, 1968, except for new credits that are judged to be essential to the financing of U. S. exports. This means that reductions through amortizations, maturities or sales may be offset by new acquisitions in these countries. However, institutions are expected to refrain from offsetting proceeds of sales to other Americans by new acquisitions from foreigners. Institutions may invest in noncovered foreign assets generally as desired. However, they are requested to refrain from making any loans and investments, noncovered as well as covered, which appear to be inconsistent with other aspects of the President's balance of payments program. Among these are the following:

1. Noncovered credits under this program that substitute directly for loans that commercial banks would have made in the absence of that part of the program applicable to them;

2. Noncovered credits to developing country subsidiaries of U. S. corporations that would not have been permitted under the Department of Commerce program if made by the U. S. parent directly.

3. Credits to U. S. corporate borrowers that would enable them to make new foreign loans and investments inconsistent with the Department of Commerce program.

4. 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.

C. Covered assets

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. Liquid funds in all foreign countries other than Canada. This category comprises 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 non-Canadian foreign obligors written, at date of acquisition, to mature in 10 years or less. This category includes bonds, notes, mortgages, loans, and other credits. 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 the Department of Defense or insured by the Foreign Credit Insurance Association, regardless of maturity.

3. Net financial investment in foreign branches, 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, any foreign businesses in which the U.S. institution has an ownership interest of 10 per cent or more. Excluded are earnings of a foreign affiliate if they are directly retained in the capital accounts of the foreign business.

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, except those acquired after September 30, 1965, in U. S. markets from American investors.[1] 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.

D. Base-date holdings

Base-date holdings for any reporting date in 1969 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), that are included in (1) but had been sold to American investors prior to the current quarter;

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[1] 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, the People's Republic of China, Cuba, Czechoslovakia, Estonia, Hungary, Communist-controlled Korea, 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 Soviet Socialist Republics, and Communist-controlled Vietnam.

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 1969, "carrying" value 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 100 per cent ceiling applies, are equal to "base-date" holdings as defined above adjusted for sales *during the current quarter* of included covered equities in accordance with the procedures specified in (2) and (3) of the preceding paragraph.

E. Noncovered assets

Foreign financial assets not covered by the guidelines are still reportable on the quarterly statistical reports to the Federal Reserve Banks. Such noncovered foreign investments include the following:

1. All financial assets in, or claims on residents of, the Dominion of Canada.

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

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

4. 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, as new gifts or, in the case of trust companies or trust departments of commercial banks, in new accounts deposited with the institution — are not defined as covered assets, if they were acquired after December 31, 1967. Such assets should be reported as a memorandum item, as should all loans held that are guaranteed or participated in by the Export-Import Bank or the Department of Defense, or insured by the Foreign Credit Insurance Association.

F. Credits to certain U.S. corporations

Any loan or investment acquired by a nonbank financial institution after June 30, 1968, that involves the advance of funds to a domestic corporation which is simply a financing conduit (commonly known as a "Delaware sub"), and which in turn will transmit the funds to a foreign business, should be reported as a foreign asset if one or more foreigners own a majority of the "Delaware" corporation. The amounts of such foreign loans or investments should be classified according to the country where the funds are actually to be used, not according to the residence of the owners of the "Delaware" corporation. In the event that U. S. residents hold a majority ownership interest in the "Delaware" corporation, no part of a loan or investment in such a corporation is to be regarded as a foreign asset of the institution.

G. Leasing of physical goods

The foreign leasing activities of firms which engage primarily in the leasing of physical assets (e.g., computers, real property, ships, aircraft), and which are not owned or controlled by a U. S. financial institution, are not reportable under the nonbank program. However, such activities are reportable when they are undertaken by nonbank financial institutions. These institutions should report the book value of any physical assets leased to foreigners on the appropriate line of the quarterly form they file with their Federal Reserve Bank.

H. Investment in certain foreign insurance ventures

Net investment in foreign insurance ventures should be reported as such wherever possible. In the case of any such ventures in which there is no segregated net investment, the U. S. insurance company may exclude from its foreign assets investments within the foreign country involved, in amounts up to 110 per cent of reserves accumulated on insurance sold to residents of that country, or (if it is larger) the minimum deposit of cash or securities required as a condition of doing insurance business within that country.

I. Long-term credits to developing-country businesses

Institutions are requested to discuss with their Federal Reserve Bank in advance any future long-term loans or direct security placements that would involve extensions of credit of $500,000 or more to private business borrowers located in the developing countries.

J. Reporting requirement

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.

Institutions with holdings below these levels, although not requested to file formal reports, are also expected to abide by the provisions of the program.

K. Covered assets in excess of ceiling

Some institutions increased, rather than reduced, their holdings of covered assets in 1968. In most such instances, there may have been special circumstances — such as inability to reduce existing investments by enough to offset new investments made to honor long-standing firm commitments or to accommodate requests for bona fide and essential financing of U. S. exports. Nevertheless, every institution whose December 31, 1968 holdings of covered assets exceeded its adjusted base-date holdings should review its situation with its Federal Reserve Bank with a view to working out an individually tailored program for eliminating the excess during 1969.

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 abroad for investment in the same country or in countries that are subject to the same or more liberal guideline limitations. Thus, funds borrowed in the developed countries of continental Western Europe may be used to finance investments in these countries and elsewhere, and funds borrowed in other developed countries (except Canada and Japan) may be used to finance investment in covered foreign assets anywhere but in the developed countries of continental Western Europe. Any institution desiring to offset foreign borrowing against foreign investment, however, should discuss its plans with the Federal Reserve Bank before entering into such an arrangement.