

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

**Circular No. 79-48
March 14, 1979**

**REGULATION K - CORPORATIONS ENGAGED IN FOREIGN BANKING
AND FINANCING UNDER THE FEDERAL RESERVE ACT**

(Proposed Amendments to Implement the International Banking Act of 1978)

**TO ALL MEMBER BANKS,
BANK HOLDING COMPANIES,
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:**

The Board of Governors of the Federal Reserve System has invited comment on a proposal to amend its Regulation K (12 C.F.R. 211) governing corporations engaged in international banking and financial operations known as Edge and "Agreement" Corporations. The amendments are designed to implement Section 3 of the International Banking Act of 1978.

At the same time, the Board has reviewed Regulation M (12 C.F.R. 213) which governs foreign operations of member banks and Section 225.4(f) of Regulation Y (12 C.F.R. 225.4(f)) which concerns foreign investment by bank holding companies. The Board proposes to incorporate revisions to these regulations in one regulation which would be entitled "International Banking Operations" and designated Regulation K.

Enclosed is a copy of the Board's press release and printed on the following pages is the proposed regulation as published in the *Federal Register*. Any comments regarding the proposal should be submitted in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. All correspondence should be received no later than April 15, 1979, and should refer to Docket No. R-0204.

Questions concerning the enclosed material should be addressed to the Attorneys' Section of our Holding Company Supervision Department, Ext. 6182.

**Sincerely yours,
Robert H. Boykin
First Vice President**

Enclosure

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[6210-01-M]

FEDERAL RESERVE SYSTEM

[Regulation K; Docket No. R-0204]

[12 CFR Part 211]

INTERNATIONAL BANKING OPERATIONS

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: Board of Governors of the Federal Reserve System proposes to revise its regulations governing the international operations of member banks, Edge and Agreement Corporations and bank holding companies. The proposal would update existing regulations and combine them in one comprehensive regulation. With respect to Edge Corporations in particular, the International Banking Act of 1978 ("IBA") directs the Board to revise its current regulation so as to further certain purposes including the stimulation of competition in providing international banking and financing services throughout the United States. The Board is required to issue final regulations by June 14, 1979. The proposed regulation implements that and other Congressional purposes contained in the IBA in addition to revising and reorganizing the Board's international banking regulations.

DATE: Comments must be received by April 15, 1979.

ADDRESS: Address comments to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. Comments should reference Docket No. R-0204.

FOR FURTHER INFORMATION CONTACT:

Frederick R. Dahl, Associate Director, Division of Banking Supervision and Regulation (202-452-2726); or C. Keefe Hurley, Jr., Senior Attorney, Legal Division (202-452-3269) Board of Governors of the Federal Reserve System.

SUPPLEMENTARY INFORMATION: The International Banking Act of 1978 (Pub. L. No. 95-369) ("IBA") requires the Board to revise its regulations governing corporations engaged in international banking and financial operations under section 25(a) of the Federal Reserve Act (12 U.S.C. 611) ("Edge Corporations"). The Board has taken this opportunity to review not only its regulations governing Edge Corporations (Regulation K, 12 CFR 211) but also its regulations governing the foreign operations of member banks (Regulation M, 12 CFR 213) and foreign investment by bank holding companies § 225.4(f) of Regulation Y, 12 CFR 225.4(f)). These regulations would be revised and combined in one

comprehensive regulation entitled "International Banking Operations" to be designated as Regulation K. Integrating these related matters into one regulation should result in better understanding of the regulation requirements.

Section 3 of the IBA contains the first significant amendment to section 25(a) of the Federal Reserve Act ("Edge Act") since the enactment of the Edge Act in 1919. In amending the Edge Act, Congress declared that Edge Corporations are to have powers sufficiently broad to enable them to compete with foreign banks in the United States as well as abroad and to provide all segments of the United States economy a means of financing international trade and, in particular, exports. In addition, Edge Corporations are to serve as a means of fostering the participation of regional and smaller banks in international banking and financing and, in general, to stimulate competition in making those services available throughout the United States.

The Board is directed to revise its regulations and policies in furtherance of these objectives. The Board is specifically directed to eliminate or modify any unnecessary restrictions that disadvantage Edge Corporations in competing foreign banks in the United States or abroad or that have the opposite effect of discriminating against foreign-owned banking institutions. Final revised regulations must be issued within 120 days of their publication for comment, or by June 14, 1979.

The Board has reviewed its regulations with several objectives in mind: first, to comply with the Congressional mandate, particularly as it relates to the United States activities of Edge Corporations; second, to eliminate obsolete restrictions and clarify remaining requirements; third, to incorporate in the regulations the policies of the Board that have previously been contained in individual interpretations and decisions; fourth, to simplify the regulatory approval process; and finally, to promote regulatory efficiency. It is intended that the revised rules will supersede the conditions now contained in individual Board consents.

As a result of this review, several areas of the regulations have been identified as being in need of significant revision. These relate to banking operations in the United States of Edge Corporations, United States offices of Edge Corporations, and regulatory approvals for foreign operations.

Banking operations in the United States. The proposed revision departs from past practice by creating a class of customer whose deposit and loan business would be presumed to be for international purposes. Those custom-

ers which, on a nonconsolidated basis, have more than two-thirds of their purchases or sales in international commerce, would be able to obtain full deposit and other banking services from Edge Corporations.

This proposal represents a significant departure from existing rules and the Board invites comment on this matter. In particular, comments are invited regarding the desirability of the qualifying customer approach, the criteria for designating an international customer, the number and size of firms that would qualify, the effects of using a different percentage, and the desirability of using a test other than purchases or sales in international commerce such as the proportion of the customer's business devoted to exports.

Under current rules and policies of the Board each deposit and credit transaction by a United States resident must be directly related to an international transaction. The Board's strict interpretation of the statutory requirement has resulted in Edge Corporations being unable to fully service, and compete effectively for the business of, firms specializing in international trade. Moreover, these rules have placed an administrative and supervisory burden on both Edge Corporations and the Federal Reserve System. The proposed approach would reduce these burdens and enlarge the ability of Edge Corporations to provide international financial services and, in this way, would be consistent with the new expression of legislative intent contained in the IBA. Those United States residents that do not qualify as international customers would continue to be able to obtain limited banking services directly connected to international transactions.

U.S. Offices of Edge Corporations. Under current regulations, Edge Corporations may establish and operate branches abroad but not in the United States. In order to provide international banking services at different locations in the United States, banks have been required to incorporate separate Edge Corporations. This requirement, by necessitating separate capitalization and separate administrations, has involved certain inefficiencies and, for some banks, has been a barrier to entering new markets.

The proposals would allow Edge Corporations to establish domestic branches with the specific prior approval of the Board. This offers the possibility of reducing costs and inconvenience associated with separate incorporation and would contribute to the efficiency and competitiveness of Edge Corporations. Allowing domestic branches of Edge Corporations would also be consistent with another directive of the IBA to make international

banking and financial services available throughout the United States. For those banks now operating Edge Corporations at several locations in the United States, the proposal would offer the possibility of a change of organizational form. Comments are requested on the proposal to allow Edge Corporations to establish branches in the United States.

Regulatory approvals. Under existing rules, prior Board consent is required for virtually all investments in foreign companies unless the investment is for less than \$500,000 and involves an ownership interest of less than 25 per cent for which a General Consent is given. In addition, prior Board approval is required for the issuance of debt obligations of more than one year maturity.

The proposed revisions contemplate the use of an expanded General Consent and prior notification, as well as specific consent procedures. The expanded General Consent would allow investments of up to \$2 million in subsidiaries and joint ventures so long as they are engaged in certain specified activities, and would allow portfolio investments in other companies up to the same dollar amount. Beyond that amount, investments could be made in subsidiaries and joint ventures engaged in specified activities up to 10 per cent of an Edge Corporation's capital with 60 days prior notice to the Board. Simplified General Consent and notification procedures would also apply to additional investments. All other investments, either involving larger amounts or activities not specified in the regulation, would require specific prior Board approval. The activities specified are those which the Board generally has allowed foreign subsidiaries to engage in because of the financial character of the activities or their relationship to international banking and financial operation. The requirement for prior approval of long-term borrowings is eliminated.

Another proposal pursuant to the IBA is that the limitation on the aggregation liabilities of Edge Corporations (currently ten times capital and surplus) be revised. All Edge Corporations will be expected to maintain adequate capital in relation to the scope and character of their operations. However, the proposal would require Edge Corporations engaged in banking to have capital and surplus of not less than six per cent of total assets. Comments are invited on the proposed capital standards.

Provisions relating to reserves against foreign branch deposits (§ 213.7 of Regulation M, 12 CFR 213.7) are being transferred to Regulation D (12 CFR 204). Rules regarding reserve requirements as they may apply to interna-

tional operations conducted by member banks and Edge and Agreement Corporations through foreign branches and subsidiaries will be considered in connection with the Board's current review of the applicability or reserve requirements under the IBA, as well as the general review of Regulation D that is in process.

As has been indicated, the IBA in amending the Edge Act emphasizes that Edge Corporations should provide to all segments of the United States economy a means of financing international trade and, in particular, exports. The proposals would further this objective by permitting Edge Corporations to finance the production of goods in the United States where the goods are to be exported. Under the current regulation, Edge Corporations may finance the shipment and storage of goods for export but not their production. In addition, by making Edge Corporations more efficient and more competitive, the proposals would promote United States' trade. The Board welcomes comments on these proposals and any suggestions that, in the terms of the IBA, would assist in achieving "a sound United States' international trade position."

The proposed revisions are intended to be comprehensive. Since the existing regulations have not been substantially amended or revised for many years, comments are invited not only on the major revisions described above but on all other parts, including those where no changes are proposed.

The proposals do not address the question of the appropriateness of foreign subsidiaries lending to United States residents for domestic purposes. In the past, the Board has generally considered this to be an impermissible activity for foreign subsidiaries on the grounds that it was not related to international business. There have been indications that the Board's interpretation is unnecessarily restrictive in that it interferes with the ability of foreign subsidiaries of Edge Corporations and member banks to compete with foreign banks. Views on this issue are requested.

Finally, under section 3(g) of the IBA, the Board is required to report to Congress recommendations on the question of whether Edge Corporations should be permitted to become members of the Federal Reserve System. Currently, the Edge Act prohibits them from becoming members even though they are required to maintain reserves on their domestic deposits. Public comment is invited in order to assist the Board in its consideration of this issue.

In developing these proposals, the Board has not followed all of the procedures set forth in its policy statement of January 15, 1979 (44 FR

3,957). The proposals were initiated before the policy statement was adopted and expeditious action is necessary to meet the statutory deadline for issuing these proposals, i.e. February 14, 1979.

For this reason, the regulatory analysis at this stage is neither as exhaustive nor as formal as that contemplated by the statement. The regulatory analysis should include at a minimum a discussion of the need for and purpose of the regulation; a description of the various options available; and an analysis, if appropriate, of their possible economic consequences; an estimate of the reporting burdens or recordkeeping requirements, and recommendations for the best course of action based on an evaluation of the alternatives.

The Board would appreciate any data and information from the public that would be of use in improving the regulatory analysis before final action is taken. Specifically, figures based on studies or surveys regarding the costs and benefits of the proposals or alternatives would be especially helpful. Conclusions should be reached as to whether the proposals or any alternatives favored by the respondents would have a major impact on:

- (1) The nation's economy as a whole e.g., an effect of \$100 million or more in gross annual costs or revenues;
- (2) Costs or prices for consumers, individual industries, levels of government or geographic regions;
- (3) The volume and cost of credit.

REGULATION K

(12 C.F.R. 211)

As amended effective

PART 211—INTERNATIONAL BANKING OPERATIONS

Sec.

- 211.1 Authority, Purpose, and Scope.
- 211.2 Definitions.
- 211.3 Foreign Branches of Member Banks.
- 211.4 Edge and Agreement Corporations.
- 211.5 Investments by Member Banks, Edge and Agreement Corporations, and Bank Holding Companies.
- 211.6 Prudential Limitations, Supervision, and Reporting.

§ 211.1 Authority, purpose, and scope.

(a) **Authority.** This part is issued by the Board of Governors of the Federal Reserve System under the authority of the Federal Reserve Act (12 U.S.C. 226) ("Act"); the Bank Holding Company Act of 1956 (12 U.S.C. 1841) ("BHCA"); and the International Banking Act of 1978 (92 Stat. 607) ("IBA").

(b) **Purpose and scope.** This Part is in furtherance of the purposes of the Act, the BHCA, and the IBA. It applies to corporations organized under section 25(a) of the Act (12 U.S.C. 611-

631), "Edge Corporations"; to corporations having an agreement or undertaking with the Board under section 25 of the Act (12 U.S.C. 601-604(a)), "Agreement Corporations"; to member banks with respect to their foreign branches and investments in foreign banks under section 25 of the Act (12 U.S.C. 601-604(a));¹ and to domestic bank holding companies with respect to the exemption from the nonbanking prohibitions of the BHCA afforded by section 4(c)(13) of the BHCA (12 U.S.C. 1843(c)(13)).

§ 211.2 Definitions.

(a) "Abroad," "foreign," or "foreign country" refers to one or more foreign nations, and includes the overseas territories, dependencies, and insular possessions of the United States, and the Commonwealth of Puerto Rico.

(b) An Edge Corporation is "engaged in banking" if it ordinarily has in the United States total deposit, acceptance, and Federal funds liabilities exceeding its capital and surplus.

(c) "Invest," "investment," and "have invested," means the purchase of shares (including rights to acquire shares) and other contributions to the capital or surplus of an organization, including the holding of an organization's subordinated debt.

(d) "Foreign bank" means an institution organized under the laws of a foreign country and any subsidiary or affiliate of the institution organized under such laws that engages in the business of banking, including merchant banking and other activities usual in connection with the business of banking, in the country where the institution is organized.

(e) "Foreign branch" means any branch located outside the country in which the parent organization is incorporated.

(f) "Organization" means a corporation, government, partnership, association, or any other legal or commercial entity.

(g) "Person" means an individual or an organization.

§ 211.3 Foreign branches of member banks.

(a) *Establishing Foreign Branches.* Prior Board approval is required for the establishment and operation of a member bank's initial branches in two foreign countries. Unless otherwise advised by the Board: (1) a member bank that has branches in two or more foreign countries may establish and operate initial branches in additional foreign countries after 60 days' prior noti-

fication to the Board; (2) without specific prior approval a member bank may establish and operate additional branches in any foreign country in which it operates one or more branches. Without 30 days a member bank shall inform the Board of the opening, closing or relocation and the address of a new or relocated branch.

(b) *Further Powers of Foreign Branches.* In addition to its general banking powers, and to the extent consistent with its charter in the case of a State bank, a foreign branch of a member bank so far as usual in connection with the business of banking in the country where it transacts business may: (1) Guarantee customers' debts or otherwise agree for their benefit to make payments on the occurrence of readily ascertainable events,² if the guarantee or agreement specifies its maximum monetary liability thereunder; but, except to the extent that the member bank is fully secured, it may not have liabilities outstanding for any person on account of such guarantees or agreements which when aggregated with other obligations of the same person exceeds the limit contained in section 5200 of the Revised Statutes (12 U.S.C. 84);

(2) Accept drafts or bills of exchange drawn upon it provided that such acceptances shall be subject to the amount limitations of section 13 of the Act (12 U.S.C. 372);

(3) Invest in the securities of the central bank, clearing houses, governmental entities, and government-owned development banks of the country in which the foreign branch is located, but the total of such investments by the branch (exclusive of securities held as required by the law of that country or as authorized under section 5136 of the Revised Statutes (12 U.S.C. 24)) shall not exceed one percent of its total deposits on the preceding year-end call report date (or on the date of acquisition in the case of a newly established branch which has not so reported);

(4) Underwrite, distribute, buy, and sell obligations of the national government of the country in which it is located (including obligations issued by any agency or instrumentality, and supported by the full faith and credit of the government). However, no member bank may hold, or be under commitment with respect to, obligations of a government as a result of underwriting, dealing, or purchasing for its own account an aggregate amount exceeding 10 percent of the member bank's capital and surplus;

(5) Take liens or other encumbrances on foreign real estate in con-

nection with its extensions of credit, whether or not of first priority and whether or not such real estate is improved or has been appraised, and without regard to maturity or amount limitations or amortization requirements of section 24 of the Act (12 U.S.C. 371);

(6) Extend credit to an executive officer of the foreign branch in an amount up to \$100,000 or its equivalent in order to finance the acquisition or construction of living quarters to be used as the officer's residence abroad, provided each credit extension is promptly reported to the branch's home office. When necessary to meet local housing costs, such amount may be exceeded with the specific prior approval of the member bank's board of directors;

(7) Act as insurance agent or broker.

A member bank that is of the opinion that other activities are usual in connection with the transaction of the business of banking in the places where its branches transact business, may apply to the Board for permission to engage in such activities.

(c) *Suspending Operations During Disturbed Conditions.* The officer in charge of a foreign branch may suspend its operations during disturbed conditions which make conduct of operations impracticable; but every effort shall be made before and during the suspension to serve the branch's depositors and customers. Full information concerning any suspension shall be reported promptly to the branch's home office, which shall immediately send a copy to the Board through the Federal Reserve Bank of its district.

(d) *Reserves.* Reserves shall be maintained against foreign branch deposits when and as required by Part 204 (Regulation D).

§ 211.4 Edge and agreement corporations.

(a) *Organization.* A proposed Edge Corporation shall become a body corporate upon issuance by the Board of a preliminary permit approving its proposed name, articles of association, and organization certificate. The name shall include "international," "foreign," "overseas," or some similar word, but may not resemble the name of another organization to an extent that might mislead or deceive the public. After issuance by the Board of a preliminary permit, an Edge Corporation may (1) elect officers and otherwise complete its organization and (2) invest in obligations of the United States Government, but none of its other powers may be exercised until the Board has issued a final permit to commence business. No amendment to the articles of association shall

¹ Although section 25 of the Act refers to national banking associations, for purposes of Federal law, the provisions of this Part apply to State member banks of the Federal Reserve System, see section 9 of the Act (12 U.S.C. 321).

² Including, but not limited to events such as nonpayment of taxes, rentals, customs duties, or costs of transport and loss of non-conformance of shipping documents.

become effective until approved by the Board.

(b) *Ownership of Shares.* Shares of stock in an Edge Corporation may not include no par value shares and shall be issuable and transferable only on its books and in compliance with section 25(a) of the Act. Any change in status of a shareholder that causes a violation of section 25(a) of the Act shall be reported to the Board as soon as possible and the Edge Corporation shall take action with respect thereto as the Board may direct. The share certificates of an Edge Corporation shall (1) name and describe each class of shares indicating its character and any unusual attributes such as preferred status of lack of voting rights; and (2) conspicuously set forth the substance of (i) limitations upon the rights of ownership and transfer of shares imposed by section 25(a) of the Act, and (ii) rules which the Edge Corporation shall prescribe in its by-laws to ensure compliance with this paragraph.

(c) *Foreign Ownership.* One or more foreign banks may apply for the Board's prior approval to acquire 50 per cent or more of the shares of the capital stock of an Edge Corporation. The Board will require a foreign bank that, in connection with such application proposed to acquire 25 per cent or more of the voting shares of an Edge Corporation, to enter into an agreement or undertaking with the Board that it will comply with the provisions of the BHCA in the same manner and to the same extent as a foreign bank that has a branch or agency in United States.

(d) *Branches.* With prior Board approval, an Edge Corporation may establish branches in the United States. An Edge Corporation may establish branches abroad in accordance with the procedures set forth in § 211.3(a). Operations of a branch abroad may be suspended during disturbed conditions in accordance with section 211.3(c).

(e) *Reserve Requirements and Interest Rate Limitations.* The liabilities of an Edge Corporation for deposits in the United States and abroad shall be subject to Parts 204 (Regulation D) and 217 (Regulation Q) in the same manner and to the same extent as if the Edge Corporation were a member bank of the Federal Reserve System.

(f) *Permissible Activities in the United States.*—(1) *General policy.* In addition to the activities described in the sixth paragraph of section 25(a) of the Act, an Edge Corporation may engage in such activities in the United States as the Board determines are incidental to its international or foreign business. The following activities will ordinarily be considered incidental to an Edge Corporation's international or foreign business:

(2) *Deposits from qualifying persons.* An Edge Corporation may receive in the United States demand, time, and savings deposits from, and issue non-negotiable certificates of deposit to:

(i) Foreign governments, persons conducting business principally at their offices or establishments abroad, and individuals resident abroad;

(ii) Persons principally engaged in international or foreign commerce. Unless the circumstances indicate otherwise, a person shall be presumed to be principally engaged in international or foreign commerce if, on an unconsolidated basis and according to documents maintained by the Edge Corporation, two thirds of the person's purchases or sales of goods and services are directly attributable to international or foreign commerce.

(3) *Deposits from other than qualifying entities.* An Edge Corporation may receive in the United States demand, time, and savings deposits and may issue nonnegotiable certificates of deposit that are not to be used to pay expenses in the United States of an office or representative if the deposits:

(i) Are to be transmitted abroad;

(ii) Consist of collateral or funds to be used for payment of extensions of credit;

(iii) Consist of the proceeds of collections abroad which funds are to be used to pay for goods exported or imported or for other costs of export or import or are to be periodically transferred to the depositor's account at another financial institution;

(iv) Consist of the proceeds of extensions of credit by the Edge Corporation; or

(v) Represent compensation to the Edge Corporation for extensions of credit or services to the customer.

(4) *Use of short term funds in the United States.* Funds of an Edge corporation not currently employed in its international or foreign business, if held or invested in the United States, shall be in the form of cash, deposits with banks, and money market instruments including bankers' acceptances, obligations of Federal, State, and local governments, Federal funds sold, and commercial paper.

(5) *Other permissible activities.* Subject to the limitations of section 25(a) of the Act and § 211.6 of this Part, an Edge Corporation may to the extent consistent with sound banking practices:

(i) Issue obligations to domestic banking offices of other banks, or to the United States or agencies thereof;

(ii) Incur indebtedness from a transfer of direct obligations that are fully guaranteed as to principal and interest by the United States or any agency thereof that the Edge Corporation is obligated to repurchase;

(iii) Issue long term subordinated debt that does not qualify as a "deposit" under Part 204 (Regulation D);

(iv) Extend credit for any purpose to a person that would be permitted to maintain deposits with the Edge Corporation under § 211.4(f)(2) where such funds are to be used in the person's business;

(v) Finance the following: (A) contracts, projects, or activities performed abroad, (B) the importation into or exportation from the United States of goods, (C) the domestic shipment or temporary storage of goods being exported or imported;

(vi) Finance the direct production and preparation of goods readily identifiable as being for export;

(vii) Take over or acquire subsequent participations in extensions of credit, or acquire obligations, growing out of transactions the Edge Corporation could have financed at inception;

(viii) Guarantee a customer's debts or otherwise agree for the customer's benefit to make payments on the occurrence of readily ascertainable events such as nonpayment of taxes, rentals, customs duties, or costs of transport and loss or nonconformance of shipping documents. The guarantee or agreement must specify the maximum monetary liability thereunder and be related to a type of transaction described in (iv)–(vi) above;

(ix) Receive checks, bills, drafts, acceptances, notes, bonds, coupons, and other securities for collection abroad, and collect such instruments in the United States for a customer abroad;

(x) Hold securities in safekeeping for, or buy and sell securities upon the order and for the account and risk of an existing customer;

(xi) Act as paying agent for securities issued by foreign governments or other entities organized under foreign law and not qualified under the laws of the United States or any State or the District of Columbia to do business in the United States;

(xii) Act as trustee, registrar, conversion agent, and paying agent with respect to any class of securities issued to finance foreign activities and distributed solely outside the United States;

(xiii) Make private placements of participations in its investments and extensions of credit; however, no Edge Corporation may otherwise engage in the business of selling or distributing securities in the United States.

(xiv) Buy and sell spot and forward foreign exchange.

(6) An Edge Corporation that is of the opinion that other activities in the United States would be incidental to its international or foreign business may apply to the Board for such a determination.

(g) *Corporations with Agreements under section 25 of the Act.* With the prior approval of the Board, a member bank may invest in a Corporation that has entered into an agreement or undertaking with the Board that it will not exercise any power except as would be permissible for an Edge Corporation under this Part.

§ 211.5 Investments in other organizations.

(a) *General Policy.* Edge Corporations, bank holding companies, and member banks (referred to in this Section as "investors"), shall confine their activities abroad to those of a banking or financial nature. In doing so, they shall at all times act in accordance with high standards of banking or financial prudence, having due regard for diversification of risks, suitable liquidity, and adequacy of capital. Subject to these considerations and the other provisions of this section, it is the Board's policy to allow activities abroad to be organized and operated as best meets corporate policies.

For purposes of this section: (i) "subsidiary" is an organization 50 per cent or more of the capital and surplus or voting stock of which is held directly or indirectly by an investor or which is otherwise controlled by an investor; (ii) "joint venture" is an organization 20 per cent or more but less than 50 per cent of the capital and surplus or voting stock of which is held directly or indirectly by an investor and which is not controlled by the investor; (iii) "portfolio investment" refers to an investment in any company other than a subsidiary or joint venture; (iv) "listed activities" means the activities contained in section 211.5(d)(1)-(13) that the Board has determined are usual in connection with the transaction of the business of banking or other financial operations abroad.

(b) *Investment limitations.* (1) In accordance with the investment procedures described in paragraph (c) of this section, an investor may:

(i) invest in a subsidiary that engages solely in listed activities or in such other activities as the Board has determined in the circumstances of a particular case are permissible;

(ii) invest in a joint venture provided that, unless otherwise permitted by the Board, not more than 5 per cent of the joint venture's consolidated assets or revenues shall be attributable to activities that would not be permissible for a subsidiary;

(iii) make portfolio investments in any organization provided that the total direct and indirect portfolio investments shall not exceed 50 per cent of the investor's capital and surplus.

(2) A member bank's direct investments shall be limited to foreign banks that: (i) are principally engaged

in a commercial banking business; (ii) are recognized as commercial banks by the bank supervisory or monetary authority of the country of their organization or principal banking operations; (iii) receive deposits to a substantial extent in the regular course of their business; and (iv) have the power to accept demand deposits. A member bank may also own or control foreign organizations that are organized for the sole purpose of either holding shares of a foreign bank or performing nominee, fiduciary or other banking services incidental to the activities of a foreign branch or foreign bank affiliate of the member bank. Investments by a foreign bank subsidiary of a member bank shall be subject to the same limitations and restrictions as an Edge Corporation.

(3) Investments by subsidiaries shall be subject to the limitations, restrictions and procedures of this section. Subsidiaries may establish branches in accordance with the procedures set forth in 211.3(a).

(4) In computing the amount which may be invested in any organization under this section there shall be included any unpaid amount for which the investor is liable and any investments by affiliated companies. The acquisition of rights to acquire shares shall be regarded as an investment; however, prior Board consent is not required for the acquisition of rights to acquire shares of an organization if such rights are acquired as an incident to an extension of credit, are exercisable only with specific Board consent, and do not cause the investor to have invested more than \$2 million in the rights and shares of the organization.

(5) An investment in an organization shall be disposed of as promptly as practicable if:

(i) the organization engages in the business of underwriting, selling or distributing securities in the United States or buying or selling goods, wares, merchandise, or commodities in the United States;

(ii) except to such limited extent as is permissible for joint ventures, a joint venture or subsidiary engages in any activity other than that which the Board has determined to be permissible; or

(iii) the investor is advised by the Board that its investment is inappropriate under the Act, the BHCA or this Part.

(c) *Investment procedures.*³ Subject to the limitations of (b) above, investments may be made in accordance with the general consent, notification, and specific consent procedures con-

³When necessary, the General Consent and prior notification provisions of this section constitute the Board's approval under the eighth paragraph of the Act for investments in excess of the limitations therein on capital and surplus.

tained in this section. The Board may at any time, upon notice, suspend the General Consent and notification procedures with respect to any investor or with respect to the acquisition of shares of companies engaged in particular kinds of activities. Each investor must receive prior specific consent of the Board for its first investment in a subsidiary, its first investment in a joint venture, and its first portfolio investment.

(1) *General Consent.* The board grants its General Consent for the following:

(A) Any investment in a joint venture or subsidiary, and any portfolio investment, provided: (i) the organization is not engaged in business in the United States; (ii) the amount invested does not exceed \$2 million or 5 per cent of the investor's capital and surplus in the case of a member bank, bank holding company or Edge Corporation engaged in banking; or (iii) \$2 million or 25 per cent of the investor's capital and surplus in the case of an Edge Corporation not engaged in banking;

(B) Additional investment in an organization in which the investor has an existing investment, provided: (i) the additional investment does not cause the investor to hold either 20 per cent or more or 50 per cent or more of the capital and surplus or voting stock of an organization being held by the investor; (ii) the additional amount invested does not in any calendar year exceed 10 per cent of the investor's original cost plus dividends for that year. The ability to make an investment pursuant to this provision of the General Consent may, if not exercised, be carried forward and accumulated for up to 5 consecutive years.

(2) *Prior Notification.* An investment (including an additional investment) in a subsidiary or joint venture that does no business in the United States and that does not qualify under the General Consent may be made after the investor has given 60 days' prior written notice to the Board provided the amount to be invested does not exceed 10 per cent of the investor's capital and surplus. The Board may, during that period, either issue a written notice disapproving the investment, extend the period or request a full application.

(3) *Specific Consent.* Any investment that does not qualify for either the General Consent or the prior notification procedure shall not be consummated without the specific prior approval of the Board.

(d) *Activities.*

(1) Commercial banking;
(2) Financing, including commercial financing, consumer financing, mortgage banking and factoring;

(3) Leasing real or personal property as is permissible for bank holding companies pursuant to section 225.4(a)(6) of Regulation Y;

(4) Acting as fiduciary;

(5) Underwriting credit life insurance and credit accident and health insurance related to extensions of credit by the investor or its affiliates;

(6) Performing services for other direct or indirect operations of a United States banking organization including representative functions, the sale of long term debt, name saving, holding assets that are acquired to prevent loss on a debt previously contracted in good faith;

(7) Holding the premises of a branch of an affiliated Edge Corporation or member bank but the amount so invested shall not exceed that which a State member bank may invest pursuant to section 24A of the Act (12 U.S.C. 371(d));

(8) Acting as investment or financial advisor to non residents of the United States;

(9) General insurance brokerage;

(10) Data processing;

(11) Managing a mutual fund, provided the fund's shares are not sold or distributed in the United States or to United States residents and the fund does not exercise any managerial control over the firms in which it invests;

(12) Performing management consulting services, provided that such services when rendered with respect to the United States market shall be restricted to the initial entry; and

(13) Underwriting, distributing and dealing in debt and equity securities outside the United States in accordance with section 211.6(a)(4) provided that, except as covered by binding commitments from subunderwriters or other purchasers, no underwriting commitment for an equity security may exceed \$2 million or represent more than 20 per cent of the capital and surplus or voting stock of any organization.

An investor that is of the opinion that other activities are usual in connection with the transaction of the business of banking or other financial operations abroad and are not inconsistent with the Act may apply to the Board for such a determination.

§ 211.6 Prudential limitations supervision and reporting.

(a) *Prudential limitations and restrictions.*—(1) *Acceptances of Edge Corporations.* An Edge Corporation shall be and remain fully secured for (i) all acceptances outstanding in excess of twice its capital and surplus, and (ii) all acceptances for any one person in excess of 10 per cent of its capital and surplus. These limitations shall not apply where the excess represents the international shipment of

goods and the Edge Corporation is fully covered by primary obligations to reimburse it which are also guaranteed by banks or bankers or where the Edge Corporation is covered by participation agreements from other banks.

(2) *Liabilities of one person.* Except as the Board may otherwise specify;

(i) The total liabilities of any person to an Edge Corporation and its direct or indirect subsidiaries shall at no time exceed 50 per cent of the Edge Corporation's capital and surplus, or 10 per cent of its capital and surplus if the Edge Corporation is engaged in banking;

(ii) The total liabilities of any person to an Edge Corporation that is a subsidiary of a member bank or to direct or indirect subsidiaries of the Edge Corporation when combined with liabilities to the member bank and its other subsidiaries shall not exceed the amount limitation on the member bank's loans to one borrower;

(iii) The total liabilities of any person to a foreign bank that is a subsidiary of a member bank shall not exceed 50 per cent of the foreign bank's capital and surplus and when combined with liabilities to the member bank and its other subsidiaries shall not exceed the amount limitation on the member bank's loans to one borrower; and

(iv) The total liabilities of any person to a foreign subsidiary of a bank holding company (other than those held through member banks and Edge Corporations) shall not exceed 50 per cent of the subsidiary's capital and surplus.

In this section, "capital and surplus" means paid in and unimpaired capital and surplus and undivided profits but does not include the proceeds of capital notes or debentures. "Subsidiary" has the same meaning as in § 211.5. "Liabilities" includes: ineligible acceptances; obligations for money borrowed; investments in another organization (valued at original cost) except where that organization is a direct or indirect subsidiary; unsecured obligations resulting from the issuance of guarantees, or similar agreements; in the case of a partnership or firm, obligations of its members; in the case of a corporation, obligations incurred for its benefit by other corporations that it controls; and in the case of a foreign government, the liabilities of its departments or agencies deriving their current funds principally from general tax revenues. "Liabilities" does not include Federal funds sold. The limitations of this paragraph shall not apply to (i) negotiable bills or drafts drawn in good faith against actual goods and on which two or more parties are liable (ii) any acceptance that has not matured and is not held by the accep-

tor, (iii) obligations to the extent secured by cash collateral or (iv) obligations to the extent supported by the full faith and credit of the following:

(1) The United States or any of its departments, agencies, establishments or wholly owned corporations (including obligations to the extent insured against foreign political and credit risks by the Export-Import Bank of the United States or the Foreign Credit Insurance Association), the International Bank for Reconstruction and Development, the International Finance Corporation, the International Development Association, the Inter-American Development Bank, or the Asian Development Bank;

(2) Any organization if at least 25 per cent of such an obligation or of the total credit is also supported by the full faith and credit of, or participated in by any institution designated in (i) above in such manner that default to the lender will necessarily include default to such institution. The total liabilities of such person shall at no time exceed 100 per cent of the capital and surplus of the lender or the parent Edge Corporation.

(3) *Capitalization.* An Edge Corporation shall at all times be capitalized in an amount that is adequate in relation to the scope and character of its activities, but in the case of an Edge Corporation engaged in banking, its capital and surplus shall not be less than six per cent of total consolidated assets.

(4) *Underwriting and dealing in securities abroad.* Where a foreign subsidiary of an Edge Corporation, member bank, or bank holding company engages in underwriting or dealing in securities, abroad pursuant to section 211.5(d), an underwriting commitment with regard to a security shall be deemed a liability of the issuer to the investor and the amount of the underwriting commitment plus other liabilities of the issuer shall not exceed the investor's lending limit.

(b) *Supervision.* Member banks, Edge Corporations and bank holding companies shall supervise and administer their foreign branches, subsidiaries and joint ventures in such a manner as to ensure that their operations conform to high standards of banking and financial prudence. Effective systems of records, controls, and reports shall be maintained to keep management informed of the activities and condition of foreign branches, subsidiaries and joint ventures. Such systems should provide, in particular, information on risk assets, liquidity management, and operations of con-

*Equity securities held in a trading or dealing portfolio are to be included when determining the aggregate amount of "portfolio investments" permitted under section 211.5.

trols and conformance to management policies. Reports on risk assets should be sufficient to permit an appraisal of credit quality and assessment of exposure to loss of the subsidiary, joint ventures, or branch, and for this purpose provide full information on the condition of material borrowers. Reports on the operations of controls should include the internal and external audits of the branch, subsidiary or joint venture. These reports and this information shall be made available to examiners of the appropriate bank supervisory agencies.

(c) *Examinations.* Examiners appointed by the Board shall examine each Edge Corporation once a year. An Edge Corporation shall make available to examiners sufficient information to assess its condition and operations and the condition and activities of any organization whose shares it holds.

(d) *Reports.* (1) Each Edge Corporation shall make at least two reports of condition annually to the Board at such times and in such form as the Board may prescribe. The Board may require that statements of condition or other reports be published or made available for public inspection.

(2) Edge Corporations, member banks, and bank holding companies shall file such reports on their foreign operations as the Board may require.

(3) A member bank, Edge Corporation or a bank holding company shall report within 30 days an acquisition or disposition of shares in a manner prescribed by the Board.

(e) *Filing procedures.* Unless otherwise directed by the Board, applications, notifications, and reports required by this Part shall be filed with the Federal Reserve Bank of the district in which the parent bank or bank holding company is located, or if none, the Federal Reserve Bank of the district in which the applying or reporting institution is located. Instructions and forms for such applications, notifications and reports are available from the Federal Reserve Bank.

By order of the Board of Governors,
February 14, 1979.

THEODORE E. ALLISON,
Secretary of the Board.

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FEDERAL RESERVE

press release

For immediate release

February 14, 1979

The Federal Reserve Board today proposed amendments to its regulations governing corporations engaged in international banking and financial operations, known as Edge Corporations. These amendments are designed to implement section 3 of the International Banking Act of 1978.

The Board also proposed a series of amendments to its regulations governing the international operations of U.S. banks. The proposals would consolidate existing regulation in this area and would formalize a number of Board policy positions that have previously been developed on a case-by-case basis.

The Board asked for comment on its proposals by April 15, 1979.

In making its proposals, the Board noted:

Section 3 of the IBA (International Banking Act) contains the first significant amendment to Section 25(a) of the Federal Reserve Act ("Edge Act") since enactment of the Edge Act in 1919. In amending the Edge Act, Congress declared that Edge Corporations are to have powers sufficiently broad to enable them to compete with foreign banks in the United States as well as abroad and to provide all segments of the United States economy a means of financing international trade, and, in particular, exports. In addition, Edge Corporations are to serve as a means of fostering the participation of regional and smaller banks in international banking and financing and, in general, to stimulate competition in making those services available throughout the United States...

The Board is specifically directed to eliminate or modify any unnecessary restrictions that disadvantage Edge Corporations in competing with foreign banks in the United States or abroad or that have the opposite effect of discriminating against foreign-owned banking institutions.

The Board has reviewed the affected regulations with the following objectives in mind:

- To comply with the Congressional mandate in the IBA, particularly as it concerns U.S. activities of Edge Corporations.
- To eliminate obsolete restrictions and to clarify the regulations.
- To incorporate into regulations Board policies previously available only in individual interpretations and decisions.
- To simplify the regulatory approval process and promote regulatory efficiency.

The principal new elements of the Board's proposals are:

1. Banking operations in the United States:

The proposed regulatory revisions would create for Edge Corporations a new class of international customer whose deposit and loan business would be presumed to be for international purposes. Customers having more than two-thirds of their purchases or sales in international commerce would qualify as international customers.

Under current rules each deposit and credit transaction by a U.S. resident with an Edge Corporation must be directly related to an international transaction. This has meant that Edge Corporations were unable to service fully, or to compete effectively for, the business of firms specializing in international trade. International customers that meet the new test would be able to conduct a full banking business with Edge Corporations. The Board specifically invited comment on this aspect of its proposal.

For all customers, Edge Corporations would be permitted to finance the production of U.S. goods for exports. Under the current regulation, Edge Corporations may finance the shipment and storage of goods for export

but not their production. The Board's proposal would be in furtherance of an IBA directive of enhancing the export financing capabilities of Edge Corporations.

2. U.S. offices of Edge Corporations:

As proposed, Edge Corporations would be allowed to establish branches in the United States with specific prior Board approval.

Under current regulations, Edge Corporations may establish branches abroad but not in the United States. To provide international banking services at different locations in the U.S., banks or other sponsors have been required to incorporate separate domestic Edge Corporations.

The proposal would be consistent with the directive in the IBA to make international banking and financial services available throughout the United States. It is intended, further, to reduce costs and inconveniences arising from multiple incorporations, to promote use of Edge Corporations by smaller and regional banks, and to contribute to the efficiency of Edge Corporations.

3. Regulatory approvals:

The Board's proposal would provide expanded and simplified procedures for investments by banks, Edge Corporations, and bank holding companies. The proposal would grant the Board's general consent for investments of up to \$2 million in foreign subsidiaries and joint ventures if they are engaged in permissible activities specified in the regulation. Consent would also be granted for limited portfolio investments in other companies.

Certain investments that do not qualify for the general consent could be made after 60 days' notification to the Board. All other investment would have to receive the Board's specific prior approval.

The activities specified in the regulation are those the Board has generally allowed foreign subsidiaries because they are of a financial character or are related to international banking and financial operations.

4. Other

The Board also proposed changes in existing limitations on the aggregate liabilities of Edge Corporations. Under the proposal, the Board stated that Edge Corporations will be expected to maintain adequate capital in relation to the scope and character of their operations but not less than 6 per cent of total assets in the case of Edge Corporations engaged in banking.

The Board's proposals do not address the question of lending by foreign subsidiaries to United States residents for domestic purposes. The Board, however, requested comment on the appropriateness of the existing policy which prohibits such loans.

The Board also requested comment on the question whether Edge Corporations should be permitted to become members of the Federal Reserve System.

The proposed regulation, which would be entitled "International Banking Operations," is attached.
