FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 79-201
December 10, 1979

REGULATION K--INTERNATIONAL BANKING OPERATIONS

Notice of Proposed Rulemaking Relating to
Interstate Banking Restrictions for Foreign Banks

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 issued proposed amendments to its Regulation K which would limit the interstate banking activities of foreign banks in the United States. This proposal would implement the provisions of the International Banking Act of 1978 which restricts the establishment of branches and subsidiary banks by a foreign bank outside its "home state". In this same action, the Board issued a proposed interpretation to Section 211.2(b) of the proposed amendments, which defines "agency" for the purposes of Regulation K.

Enclosed is a copy of the Board's press release announcing the proposal and the notices as published in the Federal Register. Any comments or views should be submitted in writing to Theodore E. Allison, Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 and should be received by January 4, 1980. All material submitted concerning the proposed amendments should include docket number R-0258 and comments regarding the proposed interpretation should reference docket number R-0259.

Any questions on the proposed amendments or interpretation should be directed to Ms. Sherry Conley, Senior Attorney, of our Holding Company Supervision Department, Ext. 6182.

Sincerely yours,

Robert H. Boykin

First Vice President

Enclosure

Banks and others are encouraged to use the following incoming WATS numbers in contacting this Bank: 1-800-442-7140 (intrastate) and 1-800-527-9200 (interstate). For calls placed locally, please use 651 plus the extension referred to above.

FEDERAL RESERVE SYSTEM

12 CFR Part 211

[Reg. K; Docket No. R-0259]

International Banking Operation; Interstate Banking Restrictions For Foreign Banks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed interpretation.

SUMMARY: The Board of Governors of the Federal Reserve System has issued an interpretation of section 211.2(b) of its proposed amendments to the Board's Regulation K (12 CFR § 211), which defines "agency" for the purposes of Regulation K.

DATE: Comments must be received by January 4, 1980.

ADDRESS: Comments, which should refer to Docket No. R-0259, may be mailed to Theodore E. Allison, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, Northwest, Washington, D.C. 20551, or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. Comments received may be inspected at Room B-1122 between 8:45 a.m. and 5:15 p.m., except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information (12 CFR § 261.6(a)).

FOR FURTHER INFORMATION CONTACT: C. Keefe Hurley, Jr., Senior Counsel (202/452-3269), or James S. Keller, Attorney (202/452-3582), Legal Division, Board of Governors of the Federal Reserve System.

SUPPLEMENTARY INFORMATION: Section 5(a) of the International Banking Act of 1978 (12 U.S.C. 3101 *et seq.*) ("IBA") provides that, with the exception of grandfathered offices, no foreign bank may directly or indirectly establish and operate either a Federal or a State branch outside its "home State" unless the foreign bank enters into an agreement or undertaking with the Board to accept only such deposits at the out-of-home State branch as would be permissible for an Edge Corporation. Under the Edge Act (12 U.S.C. 611 *et seq.*), Edge Corporations may only receive deposits in the U.S. as may be "incidental to or for the purpose of carrying out transactions in foreign countries or dependencies or insular possessions of the United States." In addition to the requirement of an agreement to restrict deposit-taking, a *Federal* branch or agency may be established or operated outside a foreign bank's home State only if the operation of such an office is expressly permitted by the receiving State, while a *State* branch, agency or commercial lending company may be established outside a foreign bank's home State only if it is approved by the bank regulatory authority of the receiving State. Subsection (a) also prohibits a foreign bank from acquiring directly or indirectly an interest in a bank located outside of the foreign bank's home State if the acquisition would be prohibited under section 3(d) of the Bank Holding Company Act ("BHCA") if the foreign bank were a bank holding company whose State of principal banking operations was the foreign bank's home State.

Subsection 5(b) grandfathers for purposes of the interstate banking restrictions, any branch, agency, bank or commercial lending company subsidiary that commenced operation or for which an application to commence business had been filed on or before July 27, 1978. Subsection 5(c) provides that the home State of a foreign bank that has any combination of branches, agencies, subsidiary lending companies, or subsidiary banks, in more than one State, is whichever State is chosen by the foreign bank (or by the Board in the event the foreign bank does not make a choice).

California offices. Section 1(b) of the IBA defines "agency" as an office that maintains credit balances but at which "deposits may not be accepted from citizens or residents of the United States," while it defines "branch" as any office "at which deposits are received." While offices of foreign banks in California have generally been prohibited from accepting deposits by a requirement of State law that such offices obtain Federal deposit insurance (an office of a foreign bank could not obtain such insurance before the passage of the IBA), California law does permit officers of foreign banks, with approval of the Banking Department, to accept deposits from any person that resides, is domiciled and maintains its principal place of business in a foreign country. Therefore, according to a literal reading of the IBA, a California office of a foreign bank that accepts deposits from certain foreign sources (e.g., a U.S. citizen residing abroad) is a branch rather than an agency. If the Board were to determine such an office, established or applied for prior to July 27, 1978, to be a branch rather than an agency, then it would be grandfathered as a branch. Accordingly, a foreign bank in this situation could elect a State other than California as its home State, obtain deposit insurance, and convert its California office to a full domestic deposit-taking facility. If, however, the Board were to determine such an office to be an "agency," then it would be grandfathered as such and could not expand its deposit-taking capabilities (unless the foreign bank selected California as its home State). The proposed interpretation indicates that, for purposes of section 5 of the IBA, the Board will regard offices of foreign banks that accept foreign source deposits, but not domestic deposits, as agencies rather than branches. Both the legislative history of section 5 of the IBA and the purposes of that section support such an interpretation. Furthermore, funds that may be received by these California offices are the type that Edge Corporations and, therefore, branches established and operated outside of a foreign bank's home State may receive. Treating these offices as agencies appears to be consistent with their method of operation and with the purpose of section 5 of the IBA.

Pursuant to its authority under the International Banking Act of 1978 (12 U.S.C. 3101 *et seq.*), the Board has issued the following interpretation of its proposed amendments to section 211.2(b) of its Regulation K:

§ 211.113 Grandfather status of certain agencies for purposes of the International Banking Act restrictions on interstate banking operations.

The Board has considered the question of whether a foreign bank's California office that may accept deposits from certain foreign sources (e.g., a United States citizen residing abroad) is a branch or an agency for the purposes of the grandfather provisions of the International Banking Act of 1978 (12 U.S.C. 3103(b)). The question has arisen as a result of the definitions in the International Banking Act of "branch" and "agency," and the limited deposit-taking capabilities of certain California offices of foreign banks.

The International Banking Act defines "agency" as "any office . . . at which deposits may not be accepted from citizens or residents of the United States," and defines "branch" as "any office . . . of a foreign bank . . . at which deposits are received" (12 U.S.C. 3101 (1) and (3)). Offices of foreign banks in California prior to the International Banking Act were generally prohibited from accepting deposits by the requirement of State law that such

offices obtain Federal deposit insurance (Cal. Fin. Code § 1756); until the passage of the International Banking Act an office of a foreign bank could not obtain such insurance. California law, however, permits offices of foreign banks, with the approval of the Banking Department, to accept deposits from any person that resides, is domiciled, and maintains its principal place of business in a foreign country (Cal. Fin. Code § 1756.2). Thus, under a literal reading of the definitions of "branch" and "agency" contained in the International Banking Act, a foreign bank's California office that accepts deposits from certain foreign sources (e.g., a U.S. citizen residing abroad), is a branch rather than an agency.

Section 5 of the IBA establishes certain limitations on the expansion of the domestic deposit-taking capabilities of a foreign bank outside its home State. It also grandfathers offices established or applied for prior to July 27, 1978, and permits a foreign bank to select its home State from among the States in which it operated branches and agencies on the grandfather date. If a foreign bank's office that was established or applied for prior to June 27, 1978, is a "branch" as defined in the International Banking Act, then it is grandfathered as a branch. Accordingly, a foreigh bank could designate a State other then California as its home State and subsequently convert its California office to a full domestic deposit-taking facility by obtaining Federal deposit insurance. If, however, the office is determined to be an "agency," then it is grandfathered as such and the foreign bank may not expand its deposit-taking capabilities in California without declaring California its home State.

In the Board's view, it would be inconsistent with the purposes and the legislative history of the International Banking Act to enable a foreign bank to expand its domestic interstate deposit-taking capabilities by grandfathering these California offices as branches because of their ability to receive certain foreign source deposits. The Board also notes that such deposits are of the same type that may be received by an Edge Corporation and, hence, in accordance with section 5(a) of the International Banking Act, by branches established and operated outside a foreign bank's home State. It would be inconsistent with the structure of the interstate banking provisions of the International Banking Act to grandfather as full deposit-taking offices those facilities whose activities have been determined by Congress to be appropriate for a foreign bank's out-of-home State branches.

Accordingly, the Board, in administering the interstate banking provisions of the IBA, regards as agencies those offices of foreign banks that do not accept domestic deposits but that may accept deposits from any person, that resides, is domiciled, and maintains its principal place of business in a foreign country.

Board of Governors of the Federal Reserve System, October 29, 1979.

Theodore E. Allison,

Secretary of the Board.

[FR Doc. 79-33833 Filed 10-31-79; 8:45 am]

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12 CFR Part 211

[Reg. K; Docket No. R-0258]

International Banking Operations; Interstate Banking Restrictions for Foreign Banks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The International Banking Act of 1978 limits the expansion of the interstate domestic deposit-taking capabilities of foreign banks by restricting the establishment of branches and subsidiary banks by a foreign bank outside of its "home State." The proposed amendments to Regulation K (International Banking Operations) implement these provisions of the International Banking Act.

DATE: Comments must be received by January 4, 1980.

ADDRESS: Comments, which should refer to Docket No. R-0258, may be mailed to Theodore E. Allison, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, Northwest, Washington, D.C. 20551, or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. Comments received may be inspected at Room B-1122 between 8:45 a.m. and 5:15 p.m., except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information (12 CFR § 261.6(a)).

FOR FURTHER INFORMATION CONTACT: C. Keefe Hurley, Jr., Senior Counsel (202/452-3269), or James S. Keller, Attorney (202/452-3582), Legal Division, Board of Governors of the Federal Reserve System.

SUPPLEMENTARY INFORMATION: Section 5(a) of the International Banking Act of 1978 (12 U.S.C. 3101 *et seq.*) ("IBA") provides that, with the exception of grandfathered offices, no foreign bank may directly or indirectly establish and operate either a Federal or a State branch outside its "home State" unless the foreign bank enters into an agreement or undertaking with the Board to accept only such deposits at the out-of-home State branch as would be permissible for an Edge Corporation (such agreement to be filed on a form provided by the Board). Under the Edge Act (12 U.S.C. 611 *et seq.*), Edge Corporations may only receive deposits in the U.S. as may be "incidental to or for the purpose of carrying out transactions in foreign countries or dependencies or insular possessions of the United States." In addition to the requirement of an agreement to restrict deposit-taking, a *Federal* branch or agency may be established or operated outside a foreign bank's home State only if the operation of such an office is expressly permitted by the receiving State, while a *State* branch, agency or commercial lending company may be established outside a foreign bank's home State only if it is approved by the bank regulatory authority of the receiving State. Subsection (a) also prohibits a foreign bank from acquiring directly or indirectly an interest in a bank located outside of the foreign bank's home State if the acquisition would be prohibited under section 3(d) of the Bank Holding Company Act ("BHCA") if the foreign bank were a bank holding company whose State of principal banking operations was the foreign bank's home State.

Subsection 5(b) grandfathers for purposes of the interstate banking restrictions any branch, agency, bank or commercial lending company subsidiary that commenced operation or for which an application to commence business had been filed on or before July 27, 1978. Subsection 5(c) provides that the home State of a foreign bank that has any combination of branches, agencies, subsidiary lending companies, or subsidiary banks, in more than one State, is whichever State is chosen by the foreign bank (or by the Board in the event the foreign bank does not make a choice).

Several issues arise in connection with the interstate restrictions of the IBA that are not addressed in the statute. The Board has attempted to resolve these issues in a manner consistent with the purposes of section 5 and its legislative history. There follows a discussion of the issues unresolved by section 5 and the Board's proposed responses.

Selection of Home State. Section 5(c) is silent as to the appropriate home State of a foreign bank that either has one deposit-taking office in the United States or is making its initial deposit-

taking entry into the United States. The statute also makes no distinction between foreign banks with deposit-taking offices (i.e. branches or subsidiary banks) and foreign banks that have have only non-deposit-taking offices (i.e. agencies or commercial lending company subsidiaries).

The legislative history of section 5 indicates Congress' intent that the home State of a foreign bank having no deposit-taking operations in the United States be the State in which that foreign bank opens its initial deposit-taking office. Conisitent with this expressed intent, the Board proposes that: (1) a foreign bank with no deposit-taking offices in the U.S., even though it may have offices in more than one State that do not take deposits, is not required to select a home State; and (2) the home State of a foreign bank with one branch or subsidiary bank, and no other offices, in the United States is the State in which that branch or subsidiary bank is located.

The Board proposes that a foreign bank with more than one office as of the grandfather date, one of which accepts domestic deposits, be required to select a home State within 90 days after the Board's regulations on this matter become final. In the event a foreign bank fails to select a home State, the Board proposes to exercice its authority to determine a foreign bank's home State. The Board proposes to use a test analogous to that used in section 3(d) of the BHCA for determining the home State of a bank holding company (that State in which the total deposits of all its banking subsidiaries is largest) to determine a foreign bank's home State. In applying this test to foreign banks, the deposits as of the latest report of condition would be determinative in the Board's designating a home State for a foreign bank that fails to do so.

Change of Home State. No provision in the IBA explicitly allows a foreign bank to change its home State. Nevertheless, it is clear from the legislative history of this section that Congress intended that the Board provide by regulation "a suitable procedure for registering with the Federal Reserve the home State and for changing it." In this regard, the most relevant consideration with respect to the change of home State for any foreign bank would be whether, and to what extent, the foreign bank has made use of its current home State to establish additional deposit-taking offices. The Board recognizes that the ability of a foreign bank to change its home State could, if unrestricted, afford a foreign bank a significant advantage over a domestic bank. A domestic bank is, for the most part, restricted to operating in the State where it is organized and, depending upon State law, may be restricted to a particular city or county. In order to afford a foreign bank some flexibility in its operations without causing competitive imbalance, the Board proposes that a foreign bank be permitted to change its home State only *once*, and that such a change in home State be conditioned upon the foreign bank: (1) either closing branches opened in reliance on its original home State designation, converting the branches to agencies or entering into an agreement with the Board regarding deposit-taking at such branches as prescribed in section 5(a) of the IBA, and (2) divesting any interests acquired in banks in reliance upon its original home State designation. This procedure would be self-implementing in that it would require notification to the Board but no Board action (unless divestiture should require a control determination under section 2(g)(3) of the BHCA).

Out-of-home State mergers. Under section 5(a) of the IBA and section 3(d) of the BHCA, a foreign bank with a subsidiary bank in one State (State X) and a branch in another State (State Y), that declares State Y as its home State is prohibited from: (1) acquiring more than 5 per cent of the shares of an additional bank in State Y (by the provisions of section 3(d) of the BHCA); or (2) acquiring more that 5 per cent of the shares of an additional bank in State X (by the provisions of section 5(a)(5) of the IBA). The Board is concerned that a foreign bank might be able to acquire an additional bank *by merger* in State X and at the same time continue to expand its deposit-taking capabilities in State Y by further branching.

The ability of a foreign bank to expand its deposit-taking capabilities significantly in more than one State appears to contravene the intent of section 5. Accordingly, the Board proposes that a foreign bank with a subsidiary bank (or banks) and branches located in different States that chooses as its home State a State other than where its subsidiary bank is located be required to give the Board 60 days' notice prior to acquiring all or substantially all of the assets of a bank outside its home State. The Board would then make a determination as to whether the foreign bank should be required to show cause as to why its home State should not be changed to the State where it subsidiary bank is located. Absent an adequate showing by the foreign bank, the home State of the foreign bank would be redesignated upon consummation of the transaction. Redesignation would require that the foreign bank terminate any domestic deposit-taking operations undertaken as a result of its original home State selection. In addition, the foreign bank would be precluded from future expansion of its domestic deposit-taking capability in its original home State. Such a procedure would enable the Board to ensure that home State selection is not used in a manner to circumvent the domestic deposit limitations of the IBA.

The factors to be considered by the Board in making its preliminary and final determinations would include: the size of the proposed acquisition relative to the foreign bank's other operations in the United States; the ability of the foreign bank to change its home State; and the existence of other potential acquirers.

Credit balances. As discussed, the interstate restrictions of the IBA were designed to limit the future deposit-taking capabilities of foreign banks. Therefore, agencies and commercial lending companies, which by law may not receive deposits, are not affected by the restrictions. Agencies do, however, receive funds in the form of credit balances, which have many of the characteristics of deposits. While the distinction between credit balances and deposits is a narrow one, it is this distinction that separates a branch from an agency. Currently each State determines the types of funds that may be maintained in the form of credit balances. Since these determinations have been made, for the most part, through the regulations or administrative practices of the State banking authorities rather than by statute, there is variation from State to State as to what constitutes a permissible credit balance. The Board is proposing, therefore, minimum criteria by which an account, if it satisfies the criteria, would be presumed to be a credit balance. The Board believes that, absent a workable Federal standard for determining whether an account at an office of a foreign bank is a credit balance or a deposit, the interstate banking restrictions of the IBA would be difficult to enforce.

The criteria proposed by the Board may be divided according to the sources of funds placed as credit balances and the uses of such accounts.

Sources. 1. Funds must be derived from the exerise of other lawful banking powers;

2. Funds must be placed in an account to serve a specific purpose; and

3. Funds may not be solicited from the general public.

Uses. 1. Accounts may not be used to pay operating expenses in the United States such as salaries, rent or taxes;

2. Funds must be withdrawn within a reasonable period of time after the specific purpose for which they were placed in the account has been accomplished; and

3. Draft usage must be reasonable in relation to the size and nature of the accounts.

These proposes minimum criteria are generally consistent with standards that have been applied by the Board as well as by States through their statutes, regulations and practices governing credit balances.

Attribution of home State. Section 5 of the IBA states that "no foreign bank may directly or *indirectly* establish and operate a Federal [or State] branch outside of its home State." Under section 2(A)(2)(a) of the BHCA, a company is considered to control a bank or another company if the company directly or indirectly has the power to vote 25 per cent or more of any class of voting shares of the bank or company. The Board believes that, in consideration of the differences between banking in foreign countries and banking in the United States, this statutory test for determining control of banks and companies should not be imposed upon foreign organizations. Rather, the Board proposes that the test for what constitutes acting indirectly be ownership or control of a majority of the voting shares of a bank. While majority ownership would be a conclusive presumption of ownership or control, the Board would reserve the right to determine administratively whether the ownership of less than a majority of the voting shares constituted acting indirectly. Under this proposal, the Board would treat as one organization entitled to one home State a foreign bank or company and its majority owned subsidiaries. Also treated as a part of the same organization would be those subsidiaries that the Board determines after notice and opportunity for a hearing are actually controlled by the foreign organization.

Pursuant to its authority under the International Banking Act of 1978 (12 U.S.C. 3101 *et seq.*), the Board proposes to amend Regulation K (12 CFR Part 211) as follows:

1. Section 211.1 (b) would be revised to read as follows:

§ 211.1 Authority, purpose, and scope.

(b) *Purpose and scope.* This Part is in furtherance of the purposes of the FRA, the BHCA, and the IBA. It applies to corporations organized under section 25(a) of the FRA (12 U.S.C. 611–631), "Edge Corporations"; to corporations having an agreement or undertaking with the Board under section 25 of the FRA (12 U.S.C. 601–604(a)), "Agreement Corporation"; to member banks with respect to their foreign branches and investments in foreign banks under section 25 of the FRA (12 U.S.C. 601–604(a));[1] to 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)); and to foreign banks with respect to the limitations on interstate banking under section 5 of the IBA (12 U.S.C. 3103).

2. Section 211.2 is amended by adding definitions of the terms "Agency," "Banking subsidiary," "Commercial lending company," and "Domestic branch," and by adding a sentence at the end of the definition of "Foreign Bank." Paragraph designations are revised where appropriate to maintain alphabetical arrangement of the terms. As amended, the section reads as follows:

§ 211.2 Definitions.

For the purposes of this part:

(a) An "affiliate"***

(b) "Agency" means any office or any place of business of a foreign bank located in any State of the United States at which credit balances are maintained, checks are paid, or money is lent but at which deposits may not be accepted from a citizen or resident of the United States. An account will not be considered a credit balance unless funds placed in the account: (1) are derived from the exercise of other lawful banking powers; (2) are to serve a specific purpose; (3) are not solicited from the general public; (4) are not used to pay operating expenses in the United States such as salaries, rent or taxes; (5) are withdrawn within a reasonable period of time after the specific purpose for which they were placed there has been accomplished; and (6) are drawn upon a manner reasonable in relation to the size and nature of the account.

(c) "Banking subsidiary," with respect to a specified foreign bank, means a United States bank that is a subsidiary as those terms are defined in section 2 of the BHCA (12 U.S.C. 1841).

(d) "Capital and surplus"***

(e) "Commercial lending company" means any institution, other than a bank or an organization operating under section 25 of the FRA, organized under the laws of any State of the United States or the District of Columbia, which maintains credit balances and engages in the business of making commercial loans. An account will not be considered a credit balance unless funds placed in the account conform to the criteria set forth in the definition of "agency" in subsection (b) of this section.

(f) "Directly or indirectly"***

(g) "Domestic branch" means any office or any place of business of a foreign bank located in any State of the United States that may accept domestic deposits and deposits that are incidental to or for the purpose of carrying out transaction in foreign countries or dependencies or insular possessions of the United States.

(h) An Edge Corporation is "engaged in banking"***

(i) "Engaged in business in the United States"***

(j) "Foreign" or "foreign country"***

(k) "Foreign bank"***. For purposes of § 211.8 of this Part, an institution organized under the laws of a foreign country that engages in the business of banking is a "foreign bank" even though all of the criteria of the preceding sentence are not satisfied.

(l) "Foreign branch"***

(m) "Investment"***

(n) "Investor"***

(o) "Joint venture"***

(p) "Listed activities"***

(q) "Organization"***

(r) "Person"***

(s) "Portfolio investment"***

(t) "Subsidiary"***

3. Regulation K would be amended by adding a new section, § 211.8, as follows:

§ 211.8 Interstate banking operations of foreign banks and foreign bank holding companies.

(a) *Determination of home State.* A foreign bank shall have its home State determined according to this section. A foreign bank that is authorized to select its home State shall do so by filing a declaration of home State within 90 days of the effective date of this section. In the absence of such selection, the Board will determine a foreign bank's home State. Within one year after the home State of a foreign bank has been determined: the foreign bank shall close its domestic branches that are not permissible under section 5(b) of the IBA or convert such domestic branches to agencies or enter into an agreement with the Board regarding deposits at such branches as prescribed in section 5(a) of the IBA and the foreign bank shall divest voting shares of, interests in or assets of banks that are not permissible under section 5(b) of the IBA.

[1] Section 25 of the FRA, which refers to national banking associations, also applies to State member banks of the Federal Reserve System by virtue of section 9 of the FRA (12 U.S.C. 321).

(1) A foreign bank that does not operate a domestic branch or banking subsidiary shall not be required to select a home State and shall not have its home State designated by the Board.

(2) A foreign bank (except a foreign bank to which subsection 4 of this section applies) that has any combination of domestic branches, banking subsidiaries, agencies, or commercial lending company subsidiaries that, before July 27, 1978, were established or applied for in more than one State may select its home State only from those States in which the foreign bank has continuously operated such offices.

(3) A foreign bank that before July 27, 1978, had established or applied for one domestic branch or one banking subsidiary, and was not otherwise engaged in banking in the United States on that date, shall have its home State determined to be the State in which such domestic branch or banking subsidiary is located.

(4) A foreign bank that before July 27, 1978, had no domestic branches or banking subsidiaries or had only agencies or commercial lending companies, and, after that date, has established or establishes either a domestic branch or a banking subsidiary shall have as its home State that State in which its initial domestic branch or banking subsidiary is located.

(b) *Change of home State.* A foreign bank may change its home State once if:

(1) Prior notification of the proposed change is filed with the Board; and

(2) Domestic branches established and investments in banks acquired in reliance on its original home State designation are conformed to that which would have been permissible had the new home State been designated as its home State originally.

(c) *Bank mergers.* (1) A foreign bank with one or more banking subsidiaries that selects as its home State a State other than that in which a banking subsidiary is located shall, if it proposes to acquire all or substantially all of the assets of a bank located outside its home State:

(i) Give 60 days' prior notification to the Board concerning the proposed acquisition, and

(ii) If the Board makes a preliminary determination that the proposed acquisition would be inconsistent with the foreign bank's home State selection, show cause why its home State should not be redesignated as a result of the proposed transaction; and

(iii) If after reviewing the foreign bank's submissions the Board makes a final determination that the proposed acquisition would be inconsistent with the foreign bank's home State selection, change it home State to the State where such acquisition is to be made in accordance with subsection (b)(2) of this section.

(2) Factors to be considered by the Board in making its preliminary and final determinations will include: the size of the proposed acquisition relative to the foreign bank's other operations in the United States; the ability of the foreign bank to change its home State; and the existence of other potential acquirers.

(d) *Attribution of home State.* (1) A foreign bank or organization and the other foreign banks or organizations over which it exercises actual control shall be regarded as one foreign bank and shall be entitled to one home State.

(2) Actual control shall be conclusively presumed to exist in the case of a bank or organization that owns or controls a majority of the voting shares of another bank or organization.

(3) Where it appears to the Board that a foreign bank or organization exercises actual control over the management or policies of another foreign bank or organization, the board may inform the parties that a preliminary determination of control has been made on the basis of the facts summarized in the communication. In the event of a preliminary determination by the Board, the parties shall within 30 days (or such longer period as may be permitted by the Board): (i) indicate to the Board a willingness to terminate the control relationship; or (ii) set forth such facts and circumstances as may support the contention that actual control does not exist (and may request a hearing to contest the Board's preliminary determination); or (iii) accede to the Board's determination in which event the parties will be regarded as one foreign bank and will be entitled to one home State.

(4) Until otherwise advised by the Board, a foreign bank or organization and any foreign bank or organization of which it owns 10 percent or more of the voting shares shall be regarded as one foreign bank entitled to one home State.

Board of Governors of the Federal Reserve System, October 29, 1979.

Theodore E. Allison,

Secretary of the Board.

[FR Doc. 79-33896 Filed 10-31-79; 8:45 am]

BILLING CODE 6210-01-M

FEDERAL RESERVE press release

For immediate release October 30, 1979

The Federal Reserve Board today proposed regulations limiting the interstate banking activities of foreign banks in the United States.

The proposed rules, on which the Board asked comment by January 4, 1980, would implement the provisions of the International Banking Act of 1978 restricting the establishment in the United States by foreign banks of branches and subsidiary banks in more than one State. The proposed rules would be incorporated into the Federal Reserve's Regulation K.

Prior to passage of the IBA, foreign banks could establish branches or agencies in one or more States, under State license. The IBA placed foreign banking in the United States under Federal regulation and established certain restrictions on the interstate operation of branches, agencies, commercial lending companies (New York investment companies) and subsidiary banks of foreign banks.

In general, the Board's proposals would prescribe procedures by which a foreign bank could choose a "home State" for its office or offices in the United States; establish rules limiting interstate expansion of domestic deposit taking by foreign banks, and provide Federal standards for distinguishing deposits from "credit balances" as a regulatory guide in limiting deposit taking by foreign banks in more than one State.

In making its proposals the Board noted that:

> The legislative history of the IBA indicates that the competitive advantage of foreign banks over domestic banks prior to passage of the IBA was most evident in the ability of foreign banks to receive domestic deposits at interstate offices.

In general, one of the purposes of the IBA is to limit the interstate domestic deposit taking capabilities of foreign banks. The Congress was less concerned with interstate lending by foreign banks, and, thus, the IBA and the Board's proposed rules do not limit such activity.

The IBA provides that the U.S. offices that foreign banks established or applied to establish as of July 27, 1978 are "grandfathered". Such foreign banks may thus continue to operate these offices. The Act provides that a foreign bank may operate domestic deposit taking offices established after the grandfather date only in its "home State".

The IBA provides further:

-- A foreign bank with offices in more than one State may choose as its home State any State in which it had, as of the grandfather date, a branch, agency, commercial lending company or a subsidiary bank. If a foreign bank does not choose a home State, the Board may do so for it.

-- Within this home State the foreign bank may expand its deposit taking activities. In other states where it has grandfathered offices it may retain those offices but not add new ones.

-- After it chooses a home State, the foreign bank may establish, elsewhere, branches or agencies that do not accept domestic deposits.

-- In the event a new out-of-home-State branch is to be established, the foreign bank must enter into an agreement with the Board that the new branch will accept only deposits such as Edge Corporations may accept: those that are incidental to or for the purpose of carrying out international transactions.

-- A foreign bank that has chosen a home State may not acquire a bank in another state.

Following are the Board's proposals with respect to these provisions of the IBA, and some of the principal considerations bearing upon the proposals.

Home State selection

1. Where a foreign bank has no deposit taking offices (branches or subsidiary banks) in the United States, the Board would not require the foreign bank to select a home State.

2. In most circumstances, the Board would accept a foreign bank's selection of a home State from among the states in which it has grandfathered offices.

3. Where a foreign bank has one branch or one subsidiary bank and no other banking offices in the United States, the State with that branch or subsidiary would be the foreign bank's home State.

4. Where a foreign bank has one or more deposit taking offices in the United States it would be required to select a home State within 90 days after the Board's regulations in this respect become final. If such a bank does not choose a home State, the Board would do so for it.

Changing a Home State

A foreign bank would be allowed to change its home State one time, provided:

-- It either closes branches it had been allowed to open due to its first home State designation, or converts such branches to agencies or to branches limited to the deposit taking authority of Edge Corporations.

-- It divests any interests it had been allowed to acquire due to its first home State designation.

Branches and Agencies

The IBA restricts the establishment of branches, but not agencies, outside a foreign bank's home State. The IBA defines a "branch" as "any office or any place of business of a foreign bank located in any State of the United States at which deposits are received." The IBA defines an "agency" as an office or place of business of a foreign bank in a State "at which credit balances are maintained . . . but at which deposits may not be accepted from citizens or residents of the United States."

Thus, the ability of an agency to receive only credit balances distinguishes an agency from a branch. Currently, the various States determine what constitutes a credit balance. To avoid a multiplicity of criteria for distinguishing credit balances from deposits, the Board proposed the following minimum criteria as a Federal standard:

1. Sources

For an account to be considered a credit balance, the funds in the account must be: derived from the exercise of other lawful banking powers; maintained at all times to serve a specific purpose, and not solicited from the general public.

2. Uses

For an account to be considered a credit balance funds in the account: must not be used to pay operating expenses in the United States, such as rent, salaries or taxes; must be withdrawn within a reasonable period of time after the specific purpose for which they were placed in the account is accomplished, and must be drawn upon in a manner reasonable in relation to the size and nature of the account.

Control of foreign bank and its affiliates

The interstate banking provisions of the IBA state that a foreign bank may not directly or indirectly establish and operate a Federal or State chartered branch outside its home State. This raises the question: what constitutes indirect control for these purposes?

The Board proposed that two or more foreign banks operating in the United States, each of which is majority owned by a common parent bank, be regarded as one banking organization, entitled to only one home State. A foreign bank and its majority owned foreign bank subsidiaries would also be regarded as one banking organization.

In making this proposal the Board recognized that it differs from the definition of a banking "family" set forth in the rules proposed by the Board under the IBA in July for the purpose of reserve requirements. The Board noted that the earlier proposal stated explicitly that the same definition of "family" may not be used for other purposes.

Acquisition by merger

The provisions of the IBA raise the question whether a foreign bank, although prohibited from acquiring directly a bank outside its home State, should also be prohibited from doing so by merger.

The Board noted that, under the Bank Holding Company Act, without application to the Board for approval a bank holding company may effectively acquire an additional bank indirectly by having its subsidiary bank acquire the assets of another bank. The Board said that this would be at odds with the general purposes of the IBA, as it would allow a foreign bank to expand its domestic deposit-taking capabilities in more than one State.

To carry out the purposes of the IBA to limit the interstate domestic deposit taking ability of foreign banks in the United States, the Board proposed:

1. To require a foreign bank holding company that has a subsidiary bank outside its home State to give 60 days notification to the Board before the subsidiary acquires all or substantially all of the assets of a bank. The Board would then examine the proposed acquisition, and determine whether it appeared to be consistent with the interstate restraints of the IBA.

If the Board decided that the resulting acquisition by merger would be contrary to the purposes of the IBA, the Board would require the foreign bank holding company to show cause why its home State designation should not be changed to that of its subsidiary bank. The foreign bank holding company would, except in the case of grandfathered offices, be required to terminate domestic deposit taking in its original home State.

2. In addition, the Board said it would support legislation that would amend the Bank Holding Company Act to forbid such acquisitions by merger.

California offices

The Board has issued a separate proposed interpretation stating that, for purposes of the interstate restrictions of the IBA, it will regard offices of foreign banks that accept foreign source deposits, but not domestic deposits, (as agencies may do under California law) as agencies rather than branches.

The Board's proposed regulations and interpretation are attached.

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