

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 81-31
February 9, 1981

INTERPRETATION OF REGULATION K

(INTERNATIONAL BANKING OPERATIONS)

Investments by United States Banking Organizations
in Foreign Companies

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 adopted an interpretation to its Regulation K concerning investments by United States banking organizations in foreign companies (including foreign banks) that do business in the United States. The interpretation applies to investments of Edge Corporations, State member banks, and bank holding companies.

Enclosed is the text of the Board's order as published in the Federal Register. Additional copies of the document may be obtained by contacting our Bank and Public Information Department, Ext. 6266.

Any questions concerning the interpretation may be directed to the Attorney's Section of our Holding Company Supervision Department, Ext. 6183.

Sincerely yours,

William H. Wallace

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**

[Docket No. R-0349; Regulation K]

International Banking Operations; Investments by United States Banking Organizations in Foreign Companies**AGENCY:** Board of Governors of the Federal Reserve System.**ACTION:** Interpretation.

SUMMARY: The Board of Governors of the Federal Reserve System has issued an interpretation describing the circumstances in which a United States banking organization will be permitted to invest in foreign companies (including foreign banks) that do domestic business in the United States.

DATE: January 19, 1981.

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

SUPPLEMENTARY INFORMATION: Edge Corporations, member banks, and bank holding companies are authorized to invest in foreign companies with the prior consent of the Board. Under the relevant statutes, however, the United States activities of the foreign company must be incidental to its international or foreign business as determined by the Board. In the past the Board has followed the policy that the United States activities of any such foreign company should, like those permitted Edge Corporations, be exclusively international in character. The Board has reviewed this policy in the light of developments in international banking and finance and the directive to improve the competitive capabilities of Edge Corporations contained in the International Banking Act of 1978.

This interpretation would permit United States banking organizations, with the prior consent of the Board, to acquire and hold interests in foreign companies (including foreign banks) that operate United States subsidiaries or direct offices that conduct domestic as well as international business. The Board would generally grant its consent where the following conditions were satisfied: (1) the foreign company is engaged predominantly in business outside the United States or in internationally related activities in the United States; (2) the direct or indirect activities of the foreign company in the United States are either banking or

closely related to banking; and (3) the United States banking organization does not own 25 per cent or more of the voting stock of, or otherwise control, the foreign company. In considering whether to grant its consent for such investments, the Board would also review the proposals to ensure that they are consistent with the purposes of the Bank Holding Company Act and the Federal Reserve Act.

Pursuant to its authority under sections 25 and 25(a) of the Federal Reserve Act (12 U.S.C. 601, 611) and section 4(c)(13) of the Bank Holding Company Act (12 U.S.C. 1843(c)(13)), the Board has issued the following interpretation with respect to the investment powers of member banks, Edge Corporations, and bank holding companies (§ 211.5 of Regulation K, 12 CFR 211.5):

§ 211.602 Investments by United States Banking Organizations in Foreign Companies that Transact Business in the United States.

Section 25(a) of the Federal Reserve Act (12 U.S.C. 611, the "Edge Act") provides for the establishment of corporations to engage in international or foreign banking or other international or foreign financial operations ("Edge Corporations"). Congress has declared that Edge Corporations are to serve the purpose of stimulating the provision of international banking and financing services throughout the United States and are to have powers sufficiently broad to enable them to compete effectively with foreign-owned institutions in the United States and abroad. The Board was directed by the International Banking Act of 1978 (12 U.S.C. 3101) to revise its regulations governing Edge Corporations in order to accomplish these and other objectives and was further directed to modify or eliminate any interpretations that impede the attainment of these purposes.

One of the powers of Edge Corporations is that of investing in foreign companies. Under the relevant statutes, however, an Edge Corporation is prohibited from investing in foreign companies that engage in the general business of buying or selling goods, wares, merchandise or commodities in the United States. In addition, an Edge Corporation may not invest in foreign companies that transact any business in the United States that is not, in the Board's judgment, "incidental" to its international or foreign business. The latter limitation also applies to investments by bank holding companies (12 U.S.C. 1843(c)(13)) and member banks (12 U.S.C. 601).

The Board has been asked to determine whether an Edge Corporation's minority investment (involving less than 25 percent of the voting shares) in a foreign company would continue to be permissible after the foreign company establishes or acquires a United States subsidiary that engages in domestic activities that are closely related to banking. The Board has also been asked to determine whether an Edge Corporation's minority investment in a foreign bank would continue to be permissible after the foreign bank establishes a branch in the United States that engages in domestic banking activities. In the latter case, the branch would be located outside the State in which the Edge Corporation and its parent bank are located.

In the past the Board, in exercising its discretionary authority to determine those activities that are permissible in the United States, has followed the policy that an Edge Corporation could not hold even a minority interest in a foreign company that engaged, directly or indirectly, in any purely domestic business in the United States. The United States activities considered permissible were those internationally related activities that Edge Corporations may engage in directly. If this policy were applied to the subject requests, the Edge Corporations would be required to divest their interests in the foreign companies notwithstanding the fact that, in each case, the Edge Corporation, as a minority investor, did not control the decision to undertake activities in the United States, and that even after the United States activities are undertaken the business of the foreign company will remain predominantly outside the United States.

International banking and finance have undergone considerable growth and change in recent years. It is increasingly common, for example, for United States institutions to have direct or indirect offices in foreign countries and to engage in activities at those offices that are domestically as well as internationally oriented. In this climate, United States banking organizations would be placed at a competitive disadvantage if their minority investments in foreign companies were limited to those companies that do no domestic business in the United States. Moreover, continued adherence to the existing policy would be contrary to the declaration in the International Banking Act of 1978 that Edge Corporations' powers are to be sufficiently broad to enable them to compete effectively in the United States and abroad. Furthermore, where the activities to be

conducted in the United States by the foreign company are banking or closely related to banking, it does not appear that any regulatory or supervisory purpose would be served by prohibiting a minority investment in the foreign firm by a United States banking organization.

In view of these considerations, the Board has reviewed its policy relating to the activities that may be engaged in in the United States by foreign companies (including foreign banks) in which Edge Corporations, member banks, and bank holding companies invest. As a result of that review, the Board has determined that it would be appropriate to interpret sections 25 and 25(a) of the Federal Reserve Act (12 U.S.C. 601, 611) and section 4(c)(13) of the Bank Holding Company Act (12 U.S.C. 1843(c)(13)) generally to allow United States banking organizations, with the prior consent of the Board, to acquire and hold investments in foreign companies that do business in the United States subject to the following conditions: (1) the foreign company is engaged predominantly in business outside the United States or in internationally related activities in the United States;* (2) the direct or indirect activities of the foreign company in the United States are either banking or closely related to banking; and (3) the United States banking organization does not own 25 percent or more of the voting stock of, or otherwise control, the foreign company. In considering whether to grant its consent for such investments, the Board would also review the proposals to ensure that they are consistent with the purposes of the Bank Holding Company Act and the Federal Reserve Act.

By order of the Board of Governors of the Federal Reserve System, January 19, 1981.

Theodore E. Allison,

Secretary of the Board.

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