



FEDERAL RESERVE BANK
OF DALLAS

ROBERT D. McTEER, JR.
PRESIDENT
AND CHIEF EXECUTIVE OFFICER

DALLAS, TEXAS
75265-5906

February 29, 1996

Notice 96-18

TO: The Chief Executive Officer of each member bank and others concerned in the Eleventh Federal Reserve District

SUBJECT

**Request for Public Comment
on a Proposed Revision to Regulation K
(International Banking Operations)**

DETAILS

The Board of Governors of the Federal Reserve System has requested public comment on a proposed revision to Regulation K (International Banking Operations) regarding the management of offshore offices by U.S. branches and agencies of foreign banks. The proposed amendments would implement a provision of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 that amended the International Banking Act of 1978 by adding a new subsection regarding the management of shell branches of foreign banks by such banks' U.S. offices.

The provision prohibits foreign banks from using their U.S. branches or agencies to manage types of activities through offshore offices that could not be managed by a U.S. bank at its foreign branches or subsidiaries. This prohibition applies to those offshore offices that are "managed or controlled" by a foreign bank's U.S. branches or agencies.

The Board must receive comments by March 25, 1996. Comments should be addressed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. All comments should refer to Docket No. R-0916.

ATTACHMENT

A copy of the Board's notice (Federal Reserve System Docket No. R-0916) is attached.

MORE INFORMATION

For more information, please contact Ann Worthy at (214) 922-6156. For additional copies of this Bank's notice, please contact the Public Affairs Department at (214) 922-5254.

Sincerely yours,

Robert D. McTeer, Jr.

FEDERAL RESERVE SYSTEM

12 CFR Part 211

[Regulation K; Docket No. R-0916]

International Banking Operations

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule and request for comments.

SUMMARY: The Board proposes to amend Regulation K to implement a provision of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Act) that amended the International Banking Act of 1978 (the IBA) by adding a new subsection regarding the management of shell branches of foreign banks by such banks' U.S. offices. The provision prohibits foreign banks from using their U.S. branches or agencies to manage types of activities through offshore offices that could not be managed by a U.S. bank at its foreign branches or subsidiaries. This prohibition applies with respect to those offshore offices that are "managed or controlled" by a foreign bank's U.S. branches or agencies.

DATE: Comments must be received on or before March 25, 1996.

ADDRESSES: Comments should refer to Docket No. R-0916, and may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, DC 20551. Comments also may be delivered to Room B-2222 of the Eccles Building between 8:45 a.m. and 5:15 p.m. weekdays, or to the guard station in the Eccles Building courtyard on 20th Street, N.W. (between Constitution Avenue and C

Street) at any time. Comments may be inspected in Room MP-500 of the Martin Building between 9:00 a.m. and 5:00 p.m. weekdays, except as provided in 12 CFR 261.8 of the Board's rules regarding availability of information.

FOR FURTHER INFORMATION CONTACT: Kathleen O'Day, Associate General Counsel (202/452-3786), Sandra L. Richardson, Managing Senior Counsel (202/452-6406), Janet S. Crossen, Senior Attorney (202/452-3281), Legal Division; Michael G. Martinson, Assistant Director, Division of Banking Supervision and Regulation (202/452-3640), Board of Governors of the Federal Reserve System. For users of Telecommunication Device for the Deaf (TDD) only, please contact Dorthea Thompson, (202/452-3544), Board of Governors of the Federal Reserve System, 20th and C Streets, N.W., Washington, DC 20551.

SUPPLEMENTARY INFORMATION: In the Interstate Act, Congress amended section 7 of the IBA (12 U.S.C. 3105) to prevent a foreign bank from using a U.S. branch or agency to manage types of activities at offshore offices that are managed or controlled by the foreign bank's U.S. branch or agency if those types of activities could not be managed by a U.S. bank at its foreign branches or subsidiaries. The proposed rule implements section 7(k) of the IBA and defines the term "managed or controlled" for purposes of the restrictions on activities set out in that section.

The Board notes that section 7(k) does not confer upon foreign banks any right to manage activities at an offshore

office from a U.S. office. The Board will continue to monitor relationships between the U.S. and offshore offices of foreign banks in the supervisory process in order to determine whether such activities are consistent with considerations relating to the safety and soundness of the U.S. operations of the foreign bank and its affiliates and compliance with law. Board staff is reviewing the use made of offshore shell branches by foreign and U.S. banks in order to gain insight into the purposes they currently serve and what, if any, supervisory risks they might pose.

Definition of "Managed and Controlled"

For purposes of the proposed rule, a non-U.S. office is considered to be "managed or controlled" by a U.S. branch or agency of a foreign bank if a majority of the responsibility for business decisions, including but not limited to decisions with regard to lending or asset management or funding or liability management, or the responsibility for recordkeeping in respect of assets or liabilities for that non-U.S. office, resides at the U.S. branch or agency. This definition is consistent with that adopted by the Federal Financial Institutions Examination Council with respect to the Supplement (FFIEC 002S) to the quarterly Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks (FFIEC 002) for the purpose of determining which U.S. branches or agencies of foreign banks "manage or control" offshore offices and thus must complete the FFIEC 002S. 57 FR 61907, Dec. 29, 1992.

In accordance with this definition, the restrictions on activities imposed by new section 7(k) of the IBA apply to those offshore offices for which a U.S. branch or agency has substantial responsibility with regard to assets or liabilities or recordkeeping. The Board considers that a determination that the restrictions apply should be made with regard to where substantive decision-making authority or responsibility for recordkeeping lies. For example, consistent with the approach taken with regard to the FFIEC 002S, a U.S. branch or agency would be deemed to "manage or control" its offshore office if (1) the manager for the U.S. branch or agency and the manager for the offshore office are the same person or there is other significant overlap in personnel; (2) substantial responsibility for decisions regarding either assets or liabilities of the offshore office resides with staff in the U.S. branch or agency; or (3) recordkeeping systems for either assets or liabilities of the offshore office are maintained in the U.S. branch or agency. The restrictions, however, generally would not apply with respect to offshore branches that are full-service facilities managed or controlled by staff located at the offshore office or at locations other than in the United States. Furthermore, the fact that an offshore office manager may report to a U.S. branch or agency manager pursuant to reporting lines established by the foreign bank will not, by itself, necessarily mean that the offshore office would be considered to be "managed or controlled"

by the U.S. branch or agency for the purposes of restrictions on activities.

Types of Activities

Section 7(k) restricts the activities that U.S. branches or agencies of foreign banks may manage through an offshore office to those types of activities that U.S. banks may manage at their foreign branches and subsidiaries, that is, those authorized under U.S. banks' state or federal charters and regulations issued by the chartering or regulatory authorities (the States, the Board, the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency). In addition, foreign branches and subsidiaries of member banks may engage in activities and make and hold investments under sections 25 and 25A of the Federal Reserve Act.

Consistent with section 7(k), the proposed amendment to Regulation K, 12 CFR Part 211, refers to the types of activities conducted and not the various procedural or quantitative supervisory requirements that may apply when a particular activity is conducted by a U.S. bank at its foreign branches or subsidiaries. Section 7(k) by its terms regulates conduct of the U.S. branch or agency of the foreign bank. It does not extend U.S. supervisory requirements to non-U.S. offices of foreign banks as such offices are not supervised or regulated by the Board. Supervision of such non-U.S. offices remains the responsibility of the home country supervisor.

Request for Comments

The Board requests comments on the proposed rule, in particular with respect to the proposed definition of "managed or controlled" and the approach contemplated for determining the types of activities that may be conducted by U.S. branches or agencies through their offshore offices.

Paperwork Reduction Act

The proposed rule does not require any "collection of information," as that term is defined in the Paperwork Reduction Act (44 U.S.C. 3501 et seq.).

Regulatory Flexibility Act Analysis

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601-612), the Board certifies that the proposed amendments will not have a significant economic impact on a substantial number of small entities.

List of Subjects in 12 CFR Part 211

Exports, Federal Reserve System, Foreign banking, Holding companies, Investments, Reporting and recordkeeping requirement.

For the reasons set out in the preamble, the Board of Governors proposes to amend 12 CFR Part 211 as set forth below.

PART 211--International Banking Operations (Regulation K)

1. The authority citation for 12 CFR Part 211 continues to read as follows:

Authority: 12 U.S.C. 221 et seq., 1818, 1841 et seq., 3101 et seq., 3901 et seq.

2. Section 211.20(b) is amended by adding a new paragraph (10) to read as follows:

§211.20 Authority, purpose, and scope.

(b) ***

(10) The management of shell branches (12 USC 3105(k)).

3. Section 211.24 is amended by adding a new paragraph (g) to read as follows:

§211.24 Approval of offices of foreign banks; procedures for applications; standards for approval; representative office activities and standards for approval; preservation of existing authority.

(g) Management of shell branches. (1) A state-licensed branch or agency shall not manage, through an office of the foreign bank which is located outside the United States and is managed or controlled by such state-licensed branch or agency, any type of activity that a bank organized under the laws of the United States or any State is not permitted to manage at any branch or subsidiary of such bank which is located outside the United States.

(2) For purposes of this subsection, an office of a foreign bank located outside the United States is "managed or controlled" by a state-licensed branch or agency if a majority of the responsibility for business decisions, including but not limited to decisions with regard to lending or asset management or funding or liability management, or the responsibility for recordkeeping in respect of assets or liabilities for that non-U.S. office, resides at the state-licensed branch or agency.

(3) The types of activities that a state-licensed branch or agency may manage through an office located outside the United States that it manages or controls include the types of activities authorized to a U.S. bank by state or federal charters, regulations issued by chartering or regulatory authorities, and other U.S. banking laws, including the Federal Reserve Act, and the implementing regulations, but U.S. procedural or quantitative requirements that may be applicable to the conduct of such activities by U.S. banks shall not apply.

By order of the Board of Governors of the Federal Reserve System, February 15, 1996.

(signed) William W. Wiles

William W. Wiles,
Secretary of the Board.