FEDERAL RESERVE BANK OF NEW YORK

[Circular No. 6087
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President's Balance of Payments Program

U. S. Department of Commerce Summary of Regulations on Foreign Direct Investment

To All Banks and Other Financial Institutions in the Second Federal Reserve District:

The following summary of the regulations on foreign direct investment was made public yesterday by the U. S. Department of Commerce:

The decision to impose mandatory controls stems from the decision that, as a part of a broader series of balance-of-payments measures, the level of direct investment outflows from the United States must be markedly reduced from recent levels.

The voluntary balance-of-payments program for corporations, which began in 1965, has been a substantial success in achieving the goals set for it. It called upon the business community (1) to cooperate in observing target limitations (stated as a percentage of capital transactions during the years 1962-64) in their foreign direct investment transactions in developed countries and (2) to maximize their over-all contributions to the balance of payments through such means as expanded exports and remittances of earnings on existing direct investments abroad through foreign borrowing.

To achieve an effective voluntary program at the lower levels of direct investment outflows now deemed necessary would be very difficult and would probably entail more inequities than a mandatory program applying uniform standards for all. Therefore, in spite of the fine cooperation of the business community in the last three years, it has been decided to institute a mandatory program under Section 95A of the Banking Act.

BASIC PROVISIONS OF THE NEW REGULATIONS

The new regulations provide three basic limitations on new investment abroad. The regulations introduce the term "direct investor," being an individual or company in the United States which owns or acquires an interest of 10 per cent or more of the voting power, earnings or capital of a foreign business venture, and the limitations are imposed, in general, on the direct investor's dealings with each of the ventures in which it has such an interest.

The regulations provide that:

(1) annual limits are placed on amounts of new transfers of capital direct investors may make in their affiliated foreign ventures;

(2) a specified share of total annual earnings from affiliated foreign ventures must be repatriated at least once each year, and

(3) the balances of short-term financial assets held abroad by direct investors with non-affiliates must be reduced by each direct investor to the average level of 1965-66.

BASIC EXCLUSIONS FROM THE SCOPE OF THE REGULATIONS

The regulations do not place limitations on:

(1) current transactions involving goods or services;

(2) purchases of portfolio securities where the total interest of the purchaser is less than 10 per cent;

(3) direct investors who do not invest or reinvest abroad more than $100,000 in each year;

(4) banks and nonbank financial institutions participating in the Federal Reserve foreign credit restraint program. The executive order gives authority to the Board of Governors to subject banks to a program similar to that set forth in the new regulations if the Board believes this action is needed to strengthen the balance of payments.

ADDITIONAL PROVISIONS OF THE REGULATIONS

Annual limits on transfers of new capital vary depending on the nationality of the foreign affiliate to which new capital is directed.

In each of three groups of countries, the limits on allowable new capital transfers for direct investment therein have been set up. The limit on such new capital transfers is measured as a percentage of the direct investor's historical investment record in these groups during a specified base period. Thus, allowable transfers of new capital to the less developed countries, when added to reinvested earnings in those countries, may not exceed in any year 110 per cent of the direct

(OVER)

investor's average investments in these less developed countries in 1965-66.

For countries in which a high level of capital inflow is essential for the maintenance of economic growth and financial stability, and where those requirements cannot be adequately met from non-United States sources—Canada, Japan, Australia, the United Kingdom and the oil-producing countries, among others—new capital transfers for direct investment, together with reinvested earnings, may not exceed 65 per cent of the average of investment in these countries in 1965-66.

For all other countries, principally Continental Western Europe (except Greece and Finland), a moratorium is imposed on any new capital outflows. However, a direct investor may reinvest annually into his ventures in these countries up to 35 per cent of the average of his total investment (transfers and reinvested earnings) during 1965 and 1966.

BORROWING ABROAD

Net long-term borrowings abroad for the purpose of financing investment abroad will not count against a direct investor's target in any of the three groups of countries. Funds made available by depreciation abroad are also not counted or required to be repatriated.

REPATRIATION REQUIREMENT

There is a requirement that in each year each direct investor repatriate from his share of the earnings of all his foreign business ventures in the three groups of countries amounts equal to the greater of (1) the same percentage of his share of total earnings from these three groups as he repatriated during 1964-66 or (2) so much of his share of earnings as may exceed the limits set for capital transfers in each group. With respect to the Continental European countries where a moratorium on capital transfers applies, the overriding rule is that earnings in excess of 35 per cent of historical investment in 1965-66 must be repatriated.

Moreover, as already noted, short-term financial assets abroad held other than in direct investments are required to be reduced to the average level of 1965 and 1966 and held at this level.

AUTHORIZATIONS

Specific authorizations will be required for any transactions subject to the regulations and not falling within the targets set up for the investor. An Office of Foreign Direct Investments in the Commerce Department has been established to administer the new regulations and will have the power to issue specific authorizations on the proper criteria.

INQUIRIES

A special staff has temporarily been assembled to handle all inquiries about the new controls. All written inquiries should be addressed to the Director, Office of Foreign Direct Investments, U. S. Department of Commerce, Washington, D. C. 20230.

As soon as the text of the regulations becomes available, we will print and send it to you.

Alfred Hayes,
President.