

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 6543]
May 19, 1970]

Changes in Guidelines for Banks Under the
President's Balance of Payments Program
Effective May 13, 1970

To All Banks in the Second Federal Reserve District:

The following statement of the Board of Governors of the Federal Reserve System has been submitted for publication in the May 1970 *Federal Reserve Bulletin*:

The Board of Governors has amended the Federal Reserve Foreign Credit Restraint Guidelines to clarify and to generalize principles developed previously in specific cases under which domestic subsidiaries of U.S. banking institutions may offset certain foreign borrowings against the foreign assets that are subject to guideline restraint.

Under the amendments, domestic subsidiaries of Edge Act and Agreement Corporations of U. S. banks, in calculating their foreign assets which are to be consolidated with those of their parents and thereby made subject to guideline ceilings, may deduct any of the subsidiaries' foreign borrowings which are outstanding and which had an original maturity of three years or more.

The principle was first laid down by the Board in April 1968, when it authorized an Edge Act Corporation to make an investment abroad through its domestic subsidiary outside the guideline ceiling to the extent it financed the investment with funds raised abroad at terms of at least 3 years. The principle has been reaffirmed in later specific authorizations. The amendment gives the principle general applicability.

The opportunity to offset foreign borrowings against foreign assets has been confined to the "second-tier" domestic subsidiaries of banks, that is, to domestic subsidiaries of Edge Act or Agreement Corporations, and not extended to banks or their Edge Act or Agreement Corporations, and has been limited to borrowings of three years or more. Such borrowings might have adverse balance-of-payments effects if, in the absence of these limits, they led to a substitution of deposits, or of short-term investments, by foreigners in the United States.

The text of the changes in the guidelines is printed on the reverse side.

Our Foreign Department (Telephone 212-732-5700, Extension 163) will be pleased to confer with you on any questions regarding the guidelines. Questions on the reports to be filed under the guidelines should be addressed to our Balance of Payments Division (Telephone 212-732-5700, Extension 8035).

Additional copies of this circular will be furnished upon request.

ALFRED HAYES,
President.

(OVER)

CHANGES IN GUIDELINES FOR BANKS

Effective May 13, 1970

II. BANKS

A. Ceilings

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7. Foreign borrowings

In principle, the restraints under these guidelines are imposed on gross foreign assets, including gross claims on foreigners. However, certain liabilities to foreigners may be counted as offsets to foreign assets only where the liabilities arise from borrowings abroad that substitute for direct investment capital outflow from the United States and are not likely to substitute for foreign deposits, or for short-term foreign investments, in the United States. Such offsetting may be done in the manner described below.

a. *Banks and Edge Act, and Agreement, Corporations.* A bank, an "Edge Act" Corporation, or an "Agreement" Corporation may not count its borrowings from, or its other liabilities to, foreigners as offsets to its claims on foreigners and other foreign assets.

b. *Domestic subsidiaries.* A domestically chartered subsidiary (for example, a so-called Delaware subsidiary) of an Edge Act Corporation or of an Agreement Corporation may count the outstanding amount of its borrowings from foreigners as offsets to its claims on foreigners and to its other foreign assets, provided those borrowings are of an original maturity of three years or more. Such borrowings would include debentures, promissory notes, or other debt obligations of the domestic subsidiary to a foreigner. The amount of the offset at any time would be equal to the amount of the outstandings after deducting (i) any repayments of principal and (ii) in the case of convertible debt issues, any conversions. This offsetting principle may be used to reduce the value of foreign assets of the subsidiary in computing the value of assets to be consolidated for reporting

purposes with those of the parent institution; any excess of outstanding borrowings of the subsidiary over foreign assets of the subsidiary may not be used to reduce the reportable value of foreign assets of the parent institution.

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D. Applicability to financial institutions

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4. Foreign branches and foreign subsidiaries of U.S. banks and banking institutions

a. The guidelines are not designed to restrict the extension of foreign credit by foreign branches of U.S. banks or by foreign subsidiaries of U.S. banks, Edge Act Corporations, or Agreement Corporations, except as the result of the restraints on banks (including Edge and Agreement Corporations) with respect to foreign credit to, or foreign investment in, such branches or subsidiaries.

b. Total claims of a bank's domestic offices on its foreign branches and foreign subsidiaries (including permanent capital invested in, as well as balances due from, such foreign branches and foreign subsidiaries) represent bank credit to foreigners for purposes of the guidelines.

5. Domestic subsidiaries of Edge Act and Agreement Corporations

The foreign assets of domestically chartered subsidiaries of Edge Act Corporations and of Agreement Corporations (net of foreign borrowings offset under II-A-7-b, above) should be consolidated with the foreign assets of the parent for purposes of the guidelines.

NOTE: The above changes consist of provisions that have been added to the guidelines sent to you with our Circular No. 6453, except that the new section II-D-4 is an amendment of the corresponding section of those guidelines and supersedes that former section.