FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 7036
November 13, 1972]

Amendments to Voluntary Foreign Credit Restraint Guidelines

Effective November 7, 1972

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

The following statement was issued November 7 by the Board of Governors of the Federal Reserve System:

The Board of Governors of the Federal Reserve System announced today the adoption of several clarifying amendments to the Voluntary Foreign Credit Restraint (VFCR) Guidelines. The revisions do not affect the foreign lending and investment ceilings of banks and other financial institutions. The amendments are essentially administrative and are designed to be neutral with respect to capital outflows under the Guidelines.

One change extends to nonbank domestic subsidiaries of bank holding companies an opportunity already afforded to domestic subsidiaries of Edge Act Corporations. That opportunity would now permit those holding company subsidiaries to reduce the amount of foreign assets charged against bank lending ceilings by the amount of outstanding borrowings they have made from foreigners for minimum maturities of three years in order to invest abroad.

In amending the provision, the Board recognized that some banks now utilize domestic subsidiaries of their holding companies to make foreign investments in the same manner as banks have been using domestic subsidiaries of Edge Act Corporations.

The Board also amended the Guidelines to incorporate several interpretations made since the present Guidelines were revised and reissued on November 11, 1971. Those amendments will:

1) specify how banks that have come into being since the end of 1970 are to calculate their lending ceilings;

2) distinguish between the characteristics of real estate investment trusts that are to be treated as nonbank financial institutions for purposes of the Guidelines and those that are not;

3) state that banks without ceilings may hold foreign assets up to $500,000 or in some cases a lower amount;

4) explain that only those trust funds over which trustees have some investment discretion and that are not separately reported by the customer are to be treated as subject to the restraints applicable to those institutions;

5) state that equity securities issued by a nonbank financial institution and sold to, and held by, foreigners in developed countries may be counted as offsets to foreign assets under ceiling in the same way that borrowings from such foreigners have been treated as offsets;

6) make clear that special adjustments for investments in foreign insurance ventures is limited only to investments made before 1965; and

7) indicate that foreign tariffs are not to be considered as part of the cost of U. S. exports for the purpose of determining an export credit.

The amendments become effective immediately.

The text of the changes in the guidelines, effective November 7, 1972, is printed on the following pages. Additional copies of this circular will be furnished upon request.

ALFRED HAYES,
President.

CHANGES IN GUIDELINES

II. BANKS

A. Ceilings for Nonexport Financing

* * *

2. *Calculation of ceilings*

A bank will have a ceiling which will be the greatest of the following:

* * *

c. 2 per cent of its total assets, as of December 31, 1970, except for a bank established on a subsequent date, 2 per cent of its total assets, month by month, until it has been in operation one full calendar year and thereafter 2 per cent of its total assets at the end of that first full calendar year of operation.

* * *

7. *Foreign borrowings*

* * *

a. *Banks, bank holding companies, Edge Act Corporations, and Agreement Corporations.* A bank, a bank holding company, 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 nonbank subsidiary (for example, a so-called Delaware subsidiary) of a bank holding company, 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 3 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 foreign 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.

* * *

E. Conformity with objectives of Guidelines

* * *

6. *Banks without ceilings*

A bank that has not adopted a ceiling will be acting in conformity with the objectives of the Guidelines (a) if its foreign assets of types subject to restraint do not exceed the lesser of (i) $500,000 or (ii) 2 per cent of its end-of-1970 total assets and (b) if those foreign assets are otherwise in conformity with the Guidelines, for example, with the request against holding funds abroad in liquid form except for necessary working balances.

* * *

III. NONBANK FINANCIAL INSTITUTIONS

A. Applicability to financial institutions

* * *

Businesses whose principal activity is the leasing of property and equipment, and which are not owned or controlled by a financial institution, are not defined as financial institutions. Real estate investment trusts whose assets consist primarily of real property as contrasted with financial assets (such as mortgages) also are not covered by these Guidelines.

* * *

D. Covered assets—subject to ceiling

* * *

7. Investments made by trust departments of commercial banks or by trust companies with trust funds over which the trustee (or co-trustee) has at least some influence over investment policy and not separately reported by another financial situation.

* * *

H. Investment in certain foreign insurance ventures

Net investment in foreign insurance ventures should be reported. In the case only of a foreign insurance venture in which a U. S. nonbank financial institution had an investment before 1965, if it is not feasible to segregate the net investment of the U. S. nonbank financial institution, the latter may exclude from its foreign assets subject to ceiling the aggregate of the larger of the following in each foreign country in which a foreign affiliate sells insurance: (a) 110 per cent of assets held in the foreign country as reserves against insurance sold to residents of that country by the foreign affiliate or (b) the minimum deposit of cash or securities required by foreign authorities as a condition of doing insurance business in that country.

* * *

J. Covered assets in excess of ceiling

1. In view of the balance of payments objectives of the program, covered investments of nonbank financial institutions may be permitted to exceed the Guideline ceiling to the extent that the funds for such investment are (a) borrowed abroad for investment in the same country or in countries that are subject to the same or more liberal Guideline restraint or (b) derive from equity securities issued by the nonbank financial institution and sold to residents of foreign developed countries (other than Canada), provided that the nonbank financial institution promptly treats as a charge against its ceiling the amount of any such equity securities at any moment it is unable to assure itself fully that any such securities continue in the possession of such foreigners.

(For reporting purposes, amount of such securities held by foreigners should be included with borrowings in foreign countries.) Thus, funds borrowed in the developed countries of continental Western Europe may be used to finance investments in these countries and elsewhere, and funds borrowed in other developed countries (except Canada) may be used to finance investment in covered foreign assets anywhere but in the developed countries of continental Western Europe. Any institution desiring to offset foreign borrowing against foreign investment, however, should discuss its plans with the Federal Reserve Bank before entering into such an arrangement.

* * *

IV. DEFINITIONS

* * *

3. "Export Credit"***

* * *

The cost of freight in connection with exportation, the cost of transport insurance in connection with exportation, and the cost of export credit guarantees and export credit insurance borne by the foreign buyer or the foreign financial institution may be included in the cost of export for the purpose of determining the amount of credit that is to be considered export credit. Any element of foreign duty is to be excluded for this purpose.