FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. **10228**
March 2, 1988]

AMENDMENT TO REGULATION K

Additional Provisions Regarding International Debt-for-Equity Swaps

To All Depository Institutions, and Others Concerned,
in the Second Federal Reserve District:

The following statement has been issued by the Board of Governors of the Federal Reserve System:

> The Federal Reserve Board announced that it has further liberalized the provisions of Regulation K to permit investments abroad by U.S. banking organizations through debt-for-equity swaps in private sector nonfinancial companies in heavily indebted developing countries.
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> The amendment is effective February 24, 1988.
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> This action is a follow-up step to the Board's revision of Regulation K in August 1987 to permit banking organizations, through debt-for-equity swaps, to own up to 100 percent of nonfinancial companies that are acquired from the government of a heavily indebted developing country.
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> The Board's regulation had already provided banking organizations with considerable flexibility to reduce exposure by selling debt to other investors or to take advantage of debt-for-equity swap programs by exchanging debt obligations for controlling equity interests in companies engaged in financial activities or portfolio investments in up to 20 percent of the shares of nonfinancial companies.
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> The Board's new amendment provides bank holding companies with broad flexibility to make investments in up to 40 percent of the shares of any private sector company in a heavily indebted developing country. The amendment also substantially lengthens the permissible holding period for investments made through debt-for-equity swaps.
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> The key elements of the amendment are:
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> - A U.S. banking organization may invest in up to 40 percent of the shares of a private sector company through a debt-for-equity swap in a heavily indebted country;
> - The U.S. banking organization that makes an investment in a private sector company under the revised regulation will also be permitted to provide loans or other financing in amounts up to 50 percent of the total loans and extensions of credit to the affiliated company;
> - The U.S. banking organization may hold the investments made through debt-for-equity swaps for two years beyond the end of the period during which full repatriation of the investment is restricted by the debtor country, up to a maximum of 15 years; and,

(OVER)

- Investments may be made under revised general consent procedures, which require no prior notice to the Board unless the size of the investment exceeds the greater of $15 million or one percent of the bank holding company's equity capital.

As a prudential measure, the amendment provides that if a bank holding company holds more than 25 percent of the voting shares of a private sector nonfinancial company, there must be another larger shareholder of the company unaffiliated with the bank holding company. In addition, the investment must be held through the bank holding company, unless the Board specifically permits the investment to be held through a bank or bank subsidiary.

These measures will add to the menu of options available to banking organizations for managing exposure to heavily indebted developing countries.

Enclosed — for depository institutions, bank holding companies, and others who maintain sets of the Board's regulations — is the complete text of the amendment to Regulation K, effective February 24, 1988, which has been reprinted from the *Federal Register* of February 24; copies will be furnished to others upon request directed to the Circulars Division of this Bank (Tel. No. 212-720-5215 or 5216). Questions regarding Regulation K may be directed to our Foreign Banking Applications Division (Tel. No. 212-720-5878).

E. Gerald Corrigan,
President.

Board of Governors of the Federal Reserve System

INTERNATIONAL BANKING OPERATIONS

AMENDMENT TO REGULATION K

(effective February 24, 1988)

FEDERAL RESERVE SYSTEM

12 CFR Part 211

[Reg. K; Docket No. R-0610]

International Banking Operations (Regulation K)

February 18, 1988.

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: After further review of its regulations and consideration of public comments,the Board has revised Regulation K governing foreign investments of U.S. banking organizations. The new regulation permits investors to acquire up to 40 percent of the shares of foreign nonfinancial companies where sovereign debt obligations are being exchanged for ownership interests in the companies. The Board also revised the regulation to permit companies acquired through debt-for-equity conversions in heavily indebted developing countries to be held for up to 15 years and liberalized the investment procedures for such investments.

EFFECTIVE DATE: February 24, 1988.

FOR FURTHER INFORMATION CONTACT: Ricki Rhodarmer Tigert, Assistant General Counsel (202–452–3428); Kathleen O'Day, Senior Counsel (202/452–3786), Legal Division; Michael G. Martinson, Assistant Director (202/452–3640); or James Keller, Manager, International Banking Applications (202/452–2523), Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve System, Washington, DC 20551. For the hearing impaired *only*, Telecommunication Device for the Deaf (TDD), Earnestine Hill or Dorothea Thompson, (202/452–3544).

SUPPLEMENTARY INFORMATION: On August 12, 1987, the Board amended Regulation K to permit investments to be made through debt-for-equity swaps in up to 100 percent of the shares of foreign nonfinancial companies, subject to certain limitations. Under the August revision to the regulation, a bank holding company may exchange sovereign debt obligations of a heavily indebted developing country for equity interests in companies being privatized by the government of the country. An investment under the August regulation must be made through a bank holding company, rather than a bank, and is required to be divested within five years, unless the time were to be extended for up to another five years. Loans made to the company are treated as investments for purposes of the investment procedures of Regulation K. The company may not bear a name similar to that of the banking organization and the bank holding company may not provide to the company any confidential information obtained from bank customers that are engaged in the same or related lines of business. In addition, the Board cautioned that, consistent with prudent banking practice, an investor should carefully evaluate the soundness of an investment before it is made, and that officer and director interlocks should be kept to as few as administratively feasible to oversee the investment.

The Board stated that its August action was the first result of its review of the area of debt-for-equity swaps. Consequently, the Board requested public comments on the revision to the regulation and stated it would consider the comments as part of its continuing evaluation of Regulation K.

The Board received 23 public comments: 18 from banks or bank holding companies, three from banking trade groups, and two from members of Congress. The comments focused generally on five areas: acquisition of private sector companies; the 10-year holding period; the requirement that the nonfinancial company be held through the holding company; the general consent procedures of Regulation K for making investments; and use of private sector debt as well as sovereign debt in making the investments. In addition, other technical comments and requests for clarification were received.

After further review of the regulation and consideration of the public comments, the Board has amended Regulation K to provide bank holding companies with greater flexibility in making debt-for-equity investments in heavily indebted developing countries. The following are the major changes to the regulation:

—A U.S. banking organization may invest in up to 40 percent of the shares of or other ownership interests in a private sector nonfinancial company through conversion of sovereign debt obligations in a heavily indebted developing country;

—If the U.S. banking organization acquires more than 25 percent of the voting shares of a nonfinancial company, another shareholder (or a control group of shareholders) would

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For this Regulation to be complete, retain:

1) Regulation K pamphlet, revised effective October 24, 1985.
2) Amendment effective July 8, 1986 (included in slip sheet dated September 1987.)
3) This slip sheet.

be required to own a larger block of shares;

—The U.S. banking organization that makes an investment in a company under the revised regulation would also be permitted to provide loans or other financing in amounts up to 50 percent of the total loans and extensions of credit to the affiliated company;

—The U.S. banking organization would be permitted to hold the investment for up to two years after the end of the period during which the debtor country restricts full repatriation of the investment, as long as the total holding period is not more than 15 years;

—The investment would be required to be held through the bank holding company and not the bank or its subsidiary, unless the Board permits a particular investment to be held through the bank; and

—The general consent limit of Regulation K (that is, the amount that an organization may invest without giving prior notice to the Board) for debt-for-equity swap investments under the revised regulation is increased to the greater of $15 million or one percent of the investor's equity capital.

A more detailed discussion of each aspect of the Board's action is provided below.

Investments in Private Sector Companies

As noted, the Board's action in August was limited to investments in public sector companies that were being privatized by the government of the foreign country. Most of the comments were favorable on the Board's decision to provide flexibility to banking organizations in dealing with their holdings of sovereign debt obligations by permitting the purchase of these companies. The commenters, however, also stated that the regulation did not go far enough and that such flexibility should be extended to allow acquisition of companies that are in the private sector. Various reasons were advanced in support of this proposal.

Most commenters noted that there are not a significant number of opportunities for investment in privatizations because many governments are reluctant to give up control of important state-owned enterprises and to allow important sectors of the economy to pass into foreign control. The amount of equity being made available for investment under privatization programs is small in relation to the amount of sovereign debt outstanding. Therefore, the commenters stated that, in order for the regulation to be meaningful, private sector companies must be eligible for investment. A number of commenters also stated that limiting debt-for-equity swap investments to companies being privatized places U.S. banking organizations at a competitive disadvantage compared to nonbanks and foreign banks, which are not subject to these limits. Moreover, some commenters said that limiting the participation of U.S. banking organizations to public sector companies will heighten competition for the few good public companies being privatized, making the investments economically less attractive.

Some commenters stated that even if controlling investments in nonfinancial private sector companies are not permitted, noncontrolling investments in greater than 20 percent of the shares of a private sector company should be allowed. Several commenters suggested permitting noncontrolling investments to be made in up to 50 percent of the shares of a company; others suggested that the permissible investment should be at least 25–30 percent of the shares of a company. The reasons advanced were that allowing a greater than 20 percent investment would permit the use of equity accounting; would put the banking organization into a better position to supervise the investment; and would make it easier to divest the company because potential investors would be more likely to want to acquire a block of shares that could give them influence over the company. These commenters also suggested that, because of the special circumstances surrounding debt-for-equity investments and their temporary nature, there should be greater leeway for a bank holding company investor to take part in the affairs of the company without the investors being considered to control the company.

The Board has revised the regulation to permit a bank holding company to hold up to 40 percent of the shares of (whether voting or nonvoting) or other ownership interests in private sector nonfinancial companies through debt-for-equity investments in heavily indebted developing countries. The Board determined that this level of equity ownership is viewed as large enough to give U.S. banking organizations a significant stake in the company, but would also a assure that there would be substantial participation by other investors. However, it is not contemplated that the U.S. banking organization would have the chief management or operating responsibility for the nonfinancial company.

This approach responds to the interest some U.S. banking organizations have expressed in making more than just portfolio investments in private sector nonfinancial companies, while also helping to assure that banking organizations do not assume all of the risks associated with operating and controlling commercial and industrial companies. By increasing the scope of investments that U.S. banking organizations may make, the liberalized regulation would enable them to diversify further their asset portfolios.

The Board placed several conditions on a bank holding company's authority to make these sizeable equity investments in nonbank companies because it continues to believe that there are significant risks in operational investments in foreign nonfinancial businesses with which bank management has little or no expertise or experience. In this regard, the Board noted that a number of banks have indicated that they are not interested in operational control over such companies and few banks have sufficient local staff to be in a position to exercise management control or supervision over a variety of business concerns. The risks associated with these investments may be exacerbated by the acquisition of the investment in a debt-for-equity swap environment where the investor may not devote the same care and attention to the acquisition because the investment is being made with funds already committed to heavily indebted countries. The experience of the Board has been that banking organizations tend to stand behind investments they have made in order to protect their own reputations in the funding markets.

In an effort to address these concerns, the regulation requires that, if a bank holding company owns more than 25 percent of the voting shares of a private sector nonfinancial company, then another shareholder (or control group of shareholders) must control a block of shares that is larger. This requirement serves a dual purpose. First, it demonstrates that there is another substantial equity holder with capital at risk. Second, because there would be a larger shareholder, the bank holding company would not bear sole operational responsibility for the company. Restricting debt-for-equity swap participation by an individual banking organization to a minority position would also help assure that this investor would not be put in a position where additional investments would be required to prop up an ailing enterprise. Restricting the level of ownership would also make it less likely that a local government might hold the U.S. organization responsible for problems caused by the nonfinancial company.

The regulation also places a limit on the amount of financing that may be provided by a bank holding company to private sector companies acquired through debt-for-equity swaps in which the bank holding company owns 20 percent or more of the voting shares (that is, above the level of share ownership in nonfinancial companies already permitted under Regulation K). Loans or other forms of financing (such as guarantees or letters of credit) are limited to not more than 50 percent of the total loans or other extensions of credit to the affiliated company. The purpose of this provision is similar to the limitation on share ownership. Because the nonfinancial company may not rely on its U.S. affiliates for all of its funding, at least half of the company's credit must be obtained in the marketplace, which would help assure that the company is creditworthy.

Such funding support from the bank, consistent with the requirements of section 23A of the Federal Reserve Act, would be permitted only where the investment is made through a direct holding company subsidiary. If, in special circumstances the Board were to permit an investment to be made through the bank or a subsidiary of the bank, additional support to the company in the form of financing by the bank would not be permitted in order to reduce risk to the bank. In assessing exposure to a company, it is realistic to look at the full range of a banking organization's financial commitments to the company. Loans would be substantially at risk, just as equity investments would be and, where an ownership interest is involved, an arms' length credit judgment is difficult to make.

Participation in major corporate decisions. The regulation provides that the bank holding company may have membership on the board of directors or on management committees of the nonfinancial company in which it invests through a debt-for-equity swap in proportion to the percentage of voting shares of the company that the bank holding company owns. In contrast with present rules on portfolio investments under Regulation K, which generally contemplate a relatively passive interest, bank holding companies could have an important voice in management of the companies through such vehicles as representation on boards of directors. In addition, there are no restrictions in the regulation on the ability of the bank holding company investor to veto major corporate actions, such as the sale or encumbrance of substantially all of the assets of the company, major mergers and acquisitions, or a dilution of shares, that could threaten the value of its investment. As noted in the comments, participation in the corporate affairs of the nonfinancial company to the extent described would allow the U.S. bank holding company to protect its investment without being in the position of exercising sole operational control over or being responsible for the company.

Holding Period

Regulation K as revised in August permitted debt-for-equity investments in nonbank companies to be held for a period of five years with the possibility of an extension for an additional five years. All comments received stated that the time period for divestiture is too short and asked that the holding period be long enough to permit the investor to maximize recovery on investments. The comments noted that all of the debt-for-equity programs in heavily indebted countries include restrictions on repatriation of dividends and on the investor's ability to sell the investment to local investors and repatriate the capital. These restrictions extend beyond the initial five years provided in the Board's regulation and in many cases beyond the 10-year maximum available with extensions under the Board's regulation.

After further review, the Board determined to permit investments made under the revised regulation to be held for the lesser of 15 years or two years beyond the end of the period established by the country restricting repatriation of the investment. This liberalization would apply to investments in public sector companies being privatized as well as to private sector companies. Extending the period to 15 years would respond to the concerns of those banking organizations that believe that divestiture will be difficult and costly if required within the period during which repatriation of the capital investment is restricted by the foreign country. Under the debt-for-equity programs of the major Latin American countries 13 years is currently the longest period during which repatriation of the investment is restricted. As a result, a maximum holding period of 15 years (or two years beyond the restricted period if shorter than 13 years) should give U.S. banking organizations greater opportunity to sell such investments.

The Board continues to emphasize that investments in nonfinancial companies are intended to be temporary, particularly where they extend beyond the periods currently permitted for investments made under authority to collect on debts previously contracted, the longest of which is five years extendable to 10 years. Therefore, banking organizations will be required to report to the Board on their plans for divestiture of debt-for-equity investments on the tenth anniversary of the acquisition of an investment and two years before the end of the holding period. This requirement would apply to investments both in private sector companies and in public sector companies being privatized. Such requirements would not apply to otherwise permissible investments even where the investments resulted from debt-for-equity swaps.

Structure for Investments

In its amendments to Regulation K in August, the Board required that the debt-for-equity investments in nonfinancial companies be held through the bank holding company and not through a subsidiary of the bank because of the potential risks to the bank from investments in commercial and industrial companies. The Board observed that the form of ownership was intended to erect a barrier between the bank and the nonbanking activities in several ways: by isolating the bank as much as possible from the activities of the nonfinancial company; by making clear that the federal safety net does not apply to the nonbanking activity; and by taking advantage of the restrictions of section 23A of the Federal Reserve Act, which apply as a matter of law to transactions between banks and affiliated nonbanks. Moreover, the approach is in keeping with the Board's position in other contexts that nonbanking activities should generally not be conducted through the bank.

The reasons that led the Board to conclude that investments in public sector nonfinancial companies being privatized should be made through the bank holding company and not the bank apply as well to investments in private sector companies. However, a number of commenters on the August revision to Regulation K contended that transferring the debt to be swapped from the bank to the holding company raises a number of problems. They stated that the bank would record an immediate loss on the transfer but the holding company would reap all of the profits from the investment. They also argued that the application of the collateral requirements of section 23A of the Federal Reserve Act to loans by the bank to a subsidiary of the holding company would serve as a disincentive to debt-for-equity investments. In addition, several commenters suggested that there are certain tax benefits to holding the investments under the bank and that local legal requirements may make it more advantageous to hold the investments through the bank.

The Board determined that these assertions do not present a compelling case for permitting nonfinancial investments to be held by the bank. As to the issue of preventing the bank from reaping profits from the investment, whether the bank shares in any profits from the investment is entirely within the control of the bank holding company. Moreover, although the holding company might gain any profits from the investments, it is also the bank holding company that would be exposed to any potential losses, thereby protecting the bank.

As to the effect of section 23A, it is intended to protect the bank from being pressured to make potentially risky loans to nonbank affiliates based on the affiliate relationship rather than the creditworthiness of the affiliated borrower. The Board determined that the protection afforded by section 23A is entirely appropriate in the context of a bank lending to foreign commercial and industrial affiliates. With respect to the tax issues, consultations with staff of the Treasury Department suggest that whether a banking organization would want to hold a nonfinancial investment under the bank, as opposed to the bank holding company, solely for tax reasons, would very must depend on the circumstances of the organization.

Accordingly, the Board required that investments by bank holding companies acquired through debt-for-equity swaps generally be held through the bank holding company. However, the Board will consider requests for exemptions on a case-by-case basis where an applicant demonstrates some special need to hold a nonfinancial investment under the bank, as, for example, in connection with local legal requirements that impose such a structure.

Investment procedures. In August, the Board did not change the investment procedures of Regulation K for debt-for-equity swaps. Several banks that commented on the Board's revision to Regulation K asked for an increase in the maximum investment under the general consent procedures from approximately $15 million to some higher figure, such as a percentage of capital, and for expedited procedures for debt-for-equity investments.

The Board determined that additional flexibility should be available in the investment procedures for debt-for-equity swaps. The regulation grants the Board's general consent for investments that do not exceed the greater of $15 million or one percent of the equity of the investing bank holding company. The Board determined that, in the context of making debt-for-equity investments where funds are already committed to a country, a percentage of the investor's equity capital is a reasonable measure of the need for review of the investments. This new limit would also apply to investments made under the previous amendment to Regulation K permitting controlling investments to be made in public sector companies.

Under the liberalized regulation, prior notice to or the specific consent of the Board will be required where (1) the amount to be invested exceeds the greater of $15 million or one percent of the investor's equity capital after the deduction of goodwill; (2) the country's debt-for-equity swap program requires the investor to invest new money in addition to swapping debt obligations, and then only if the new money portion of the investment exceeds $15 million; or (3) the investment is to be made through an insured bank or its subsidiary.

Use of private sector debt. The Board's August revision to Regulation K provided that the debt that is eligible to be swapped is sovereign debt of the heavily indebted developing countries. A number of commenters asked that all debt eligible for swapping under the various country programs should also be eligible under the Board's regulations. They stated that some country programs restrict the debt eligible for swapping and that the Board should not disadvantage U.S. banking organizations by further restricting the debt eligible for use. Rather, they stated that banking organizations should have the flexibility to swap any type of debt, regardless of the sector of the borrower.

Although the Board considered these comments, it determined that the regulation should continue to permit the use only of sovereign debt. The Board began its review and liberalization of debt-for-equity investments in order to provide banks with flexibility in dealing with their holdings of sovereign debt and continues to believe that this is an appropriate limitation. This is especially true in light of the fact that banking organizations already have other authorities to collect on debts previously contracted where the debt is in default. Sovereign debt does not fall within this category and therefore requires alternative approaches, such as the revised regulation.

Some commenters also requested clarification of what constitutes sovereign debt. It is contemplated that sovereign debt includes debts owed to or fully guaranteed by governments and their agencies and instrumentalities.

Definition of "investment." In its August amendment to Regulation K the Board defined the term "investment" for purposes of the Board's procedures for prior notice and review of investments to include extensions of credit by the investing bank holding company or its affiliates. This approach gives the Board an opportunity to examine the level of a U.S. banking organization's financial support for a foreign company from a safety and soundness perspective where the amounts are large. The Board determined that this requirement should apply to all debt-for-equity investments, including those in private sector nonfinancial companies.

Accounting for debt-for-equity investments. Under Generally Accepted Accounting Principles (GAAP) a U.S. banking organization that holds 20 percent or more of the shares of a company should generally use consolidation or equity accounting to reflect in its income statement undistributed earnings as well as dividends received from the company. However, GAAP also provides that the cost method of accounting should be used where there are severe restrictions on the ability of the organization to realize income from, or the principal of, an investment, or where the investment is likely to be temporary.

It appears that some banks want to be able to invest in 20 percent or more of the shares of nonfinancial companies in order to be able to use equity accounting for the investment, even though the investment would be temporary and would be subject to restrictions on repatriation of investments and dividends. In fact, some commenters cited the ability to use equity accounting as one of the reasons why the Board should permit larger percentage investments in nonfinancial companies. In contrast, other banking organizations intend to use cost accounting under which income is recognized essentially in the same accounting period in which the money is actually received.

Any banking organization considering the use of equity accounting for investments made through debt-for-equity swaps in heavily indebted countries should carefully evaluate whether that method of accounting would result in an accurate statement of the income and capital of the banking organization.

Other Comments

Several requests for clarification of the procedures for debt-for-equity investments were received. Debt-for-equity investments may continue to be made under other provisions of Regulation K. The requirements of § 211.5(f) must be followed only if the investment would not otherwise be permitted under § 211.5 (c) and (d) of Regulation K. Similarly, any investment acquired through a debt-for-equity swap must be divested only if it is not otherwise permissible for the bank holding company to own at the end of the divestiture period.

The investments permitted by the revised regulation may be made through an Edge corporation subsidiary of a bank holding company as long as the Edge corporation is not a subsidiary of an insured bank.

Regulatory Flexibility Analysis

Pursuant to section 605(b) of the Regulatory Flexibility Act (Pub. L. 96–354; 5 U.S.C. 601 *et seq.*), the Board of Governors of the Federal Reserve System certifies that the amendment will not have a significant economic impact on a substantial number of small entities that would be subject to the regulation. The amendment would liberalize existing regulations and affects only those banking organizations engaged in international banking. It would not have any particular effect on small business entities.

The Board has determined that the provisions of section 553(b) of Title 5, United States Code, with respect to deferred effective date are not necessary with respect to this revision to Regulation K. As noted above, this amendment liberalizes the investment restrictions of the regulation. An immediate effective date will allow banking organizations to begin to make investments under the revised provisions upon publication in the Federal Register.

List of Subjects in 12 CFR Part 211

Banks, Banking, Federal Reserve System, Foreign banking, Investments, Reporting and recordkeeping requirements, Export trading companies, Allocated transfer risk reserve, Reporting and disclosure of international assets, Accounting for fees on international loans, Investment made through debt-for-equity conversions.

For the reasons set forth above, the Board amends 12 CFR Part 211 as follows:

PART 211—INTERNATIONAL BANKING OPERATIONS

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

Authority: Federal Reserve Act (12 U.S.C. 221 *et seq.*); Bank Holding Company Act of 1956, as amended (12 U.S.C. 1841 *et seq.*); the International Banking Act of 1978 (Pub. L. 95–369); 92 Stat. 607; 12 U.S.C. 3101 *et seq.*); the Bank Export Services Act (Title II, Pub. L. 97–290, 96 Stat. 1235); and the International Lending Supervision Act (Title IX, Pub. L. 98–181, 97 Stat. 1153, 12 U.S.C. 3901 *et seq.*), unless otherwise noted.

2. Section 211.5 is amended by revising paragraph (f) to read as follows.

§ 211.5 Investments and activities abroad.

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(f) *Investments made through debt-for-equity conversions*—(1) *Definitions.* For purposes of this paragraph:

(i) "Eligible country" means a country that, since 1980, has restructured its sovereign debt held by foreign creditors, and any other country the Board deems to be eligible;

(ii) "Equity" includes common stockholder's equity and minority interests in consolidated subsidiaries, less goodwill;

(iii) "Investment" has the meaning set forth in § 211.2(i) of this regulation and, for purposes of the investment procedures of this paragraph only, shall include loans or other extensions of credit by the bank holding company or its affiliates to a company acquired pursuant to this paragraph;

(iv) "Loans and extensions of credit" means all direct and indirect advances of funds to a person made on the basis of any obligation of that person to repay the funds.

(2) *Permissible investments.* In addition to investments that may be made under other provisions of this section, a bank holding company may make the following investments through the conversion of sovereign debt obligations of an eligible country, either through direct exchange of the debt obligations for the investment or by a payment for the debt in local currency, the proceeds of which are used to purchase the investment:

(i) *Public sector companies.* A bank holding company may acquire up to and including 100 percent of the shares of (or other ownership interests in) any foreign company located in an eligible country if the shares are acquired from the government of the eligible country or from its agencies or instrumentalities.

(ii) *Private sector companies.* A bank holding company may acquire up to and including 40 percent of the shares, including voting shares, of (or other ownership interests in) any other foreign company located in an eligible country subject to the following conditions:

(A) A bank holding company may acquire more than 25 percent of the voting shares of the foreign company only if another shareholder or control group of shareholders unaffiliated with the bank holding company holds a larger block of voting shares of the company;

(B) The bank holding company and its affiliates may not lend or otherwise extend credit to the foreign company in amounts greater than 50 percent of the total loans and extension of credit to the foreign company; and

(C) The bank holding company's representation on the board of directors or on management committees of the foreign company may be no more than proportional to its shareholding in the foreign company.

(3) *Investments by bank subsidiary of bank holding company.* Upon application, the Board may permit an investment to be made pursuant to this paragraph through an insured bank subsidiary of the bank holding company where the bank holding company demonstrates that such ownership is necessary due to special circumstances such as the requirements of local law. In granting its consent, the Board may impose such conditions as it deems necessary or appropriate to prevent adverse effects, including prohibiting loans from the bank to the company in which the investment is made.

(4) *Divestiture*—(i) *Time limits for divestiture.* The bank holding company shall divest the shares of or other ownership interests in any company acquired pursuant to this paragraph (unless the retention of the shares or other ownership interest is otherwise permissible at the time required for divestiture) within two years of the date on which the bank holding company is permitted to repatriate in full the investment in the foreign company, but in any event within 15 years of the date of acquisition.

(ii) *Report to Board.* The bank holding company shall report to the Board on its plans for divesting an investment made under this paragraph no later than 10 years after the date the investment is made if the investment may be held for longer than 10 years and shall report to the Board again two years prior to the final date for divestiture, in a manner to be prescribed by the Board.

(iii) *Other conditions requiring divestiture.* All investments made pursuant to this paragraph shall be subject to paragraphs (b)(3)(i) (A) and (B) of this section requiring prompt divestiture (unless the Board upon application authorizes retention) if the company invested in engages in impermissible business in the United States.

(5) *Investment procedures*—(i) *General consent.* Subject to the other limitations of this paragraph, the Board grants its general consent for investments made under this paragraph if the total amount invested does not exceed the greater of $15 million or one percent of the equity of the investor.

(ii) All other investments shall be made in accordance with the procedures of paragraph (c) of this section requiring prior notice or specific consent.

(6) *Conditions*—(i) *Name.* Any company acquired pursuant to this paragraph shall not bear a name similar to the name of the acquiring bank holding company or any of its affiliates.

(ii) *Confidentiality.* Neither the bank holding company nor its affiliates shall provide to any company acquired pursuant to this paragraph any confidential business information or other information concerning customers that are engaged in the same or related lines of business as the company.

Board of Governors of the Federal Reserve System, February 18, 1988.

William W. Wiles,

Secretary of the Board.

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