NOTES

THE INTERNATIONAL BANKING ACT OF 1978: FEDERAL REGULATION OF FOREIGN BANKS IN THE UNITED STATES*

I. INTRODUCTION

The United States has recently experienced a tremendous increase in foreign banking activity.[1] In response to this increased activity, Congress has been evaluating the regulatory role which the federal government should take in order to accommodate this growth effectively. The International Banking Act of 1978 (IBA)[2] is the most recent congressional proposal for federal regulation of foreign banks in the United States.[3]

The growth of foreign banks in the United States has been directly related to the increased volume of foreign trade and investment in this

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[1] The number of foreign bank facilities in the United States has increased 101%, from 104 to 210, in the past five years, and during the same period foreign bank assets have experienced an even greater growth of 172%, from $24 billion to $66 billion. This growth is measured from January 1972 to April 1977. While this growth has been dramatic, it is relatively small when compared to the United States banking involvement in foreign countries. *International Banking Act of 1977: Hearings on H.R. 7325 Before the Subcomm. on Financial Institutions Supervision, Regulation and Insurance of the House Comm. on Banking, Finance and Urban Affairs*, 95 Cong., 1st Sess. 573 (1977) (statement of Robert Bloom) [hereinafter cited as *Int'l Banking Act of 1977, House Hearings*]. *See generally* D'Arista, *The Foreign Bank Invasion*, 160 BANKER'S MAGAZINE 43 (1977); HOUSE COMM. ON BANKING, CURRENCY AND HOUSING, 94TH CONG., 2D SESS., COMPENDIUM OF PAPERS PREPARED FOR THE FINE STUDY, BK. II, PT. 4, INTERNATIONAL BANKING 727 (Comm. Print 1976) [hereinafter cited as INTERNATIONAL BANKING].

[2] H.R. 10899, 95th Cong., 2d Sess., 124 CONG. REC. 1602 (1978), [hereinafter cited as *Int'l Banking Act of 1978*].

[3] Previous proposals were made in 1975 (*Foreign Bank Act of 1975: Hearings on S. 958 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. (1976) [hereinafter cited as *Foreign Bank Act of 1975, Senate Hearings*]), in 1976 (*International Banking Act of 1976: Hearings on H.R. 13876 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. (1976) [hereinafter cited as *Int'l Banking Act of 1976, Senate Hearings*]), and in 1977 (*Int'l Banking Act of 1977, House Hearings, supra* note 1). Testimony at the 1977 hearings resulted in extensive revisions to the original bill as presented to the House. A revised bill incorporating the changes was issued in Committee Print on October 13, 1977. SUBCOMM. ON FINANCIAL INSTITUTIONS SUPERVISION, REGULATION AND INSURANCE OF THE HOUSE COMM. ON BANKING, FINANCE AND URBAN AFFAIRS, 95TH CONG., 1ST SESS. INTERNATIONAL BANKING ACT OF 1977, H.R. 7325 (Comm. Print 1977) [hereinafter cited as Comm. Print]. This Committee Print was introduced verbatim to the second session of the 95th Congress on February 9, 1978 as *Int'l Banking Act of 1978, supra* note 2. It is this Committee Print, however, which this Note refers to as the International Banking Act of 1978 (IBA) and upon which the analysis in this Note is based.

country,[4] attributable in part to the increasing attraction of foreign countries to the United States as an international market.[5] Furthermore, this growth of foreign bank entry into the United States is part of a global trend towards transnational banking which is expected to continue. In response to the continued growth of foreign banks in the United States, Arthur Burns, then Chairman of the Federal Reserve Board (FRB), commented:

> From the Board's standpoint, we are primarily concerned about the absence of national policy and regulatory framework in this increasingly important area and its attendant ramifications for the formulation of monetary policy, the development of a sound and competitive banking system, and the coordination of policies with national monetary and regulatory authorities abroad.[6]

This Note examines the advantages and disadvantages of federal regulation of foreign banking and analyzes the effectiveness of the regulatory proposals made in the IBA. In addition, the present regulatory system will be discussed in relation to its effect on foreign banks and their organizational structure.

II. THE UNITED STATES REGULATORY ENVIRONMENT

A. *Domestic Environment*

Our "baffling banking system"[7] involves multiple regulatory entities and

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[4] The development of foreign banking in the United States can be traced to substantial foreign investment in the mid-nineteenth century. Canada and Japan were the first countries to initiate foreign banking in the United States by opening facilities in California in the 1870's. Foreign banking then responded to the economic climate of the United States by surging after World War I, plummeting during the Depression years, and reviving again after World War II.

As international trade increased, foreign banks realized a need to establish American facilities to handle related banking transactions. Likewise, certain American banks opened branch offices in foreign countries. As these international transactions increased American banks met increasing foreign resistance, based upon the complaint that United States authorities did not provide reciprocal opportunities for foreign banks wanting to establish branches in the United States. In light of the threat of foreign retaliation against United States banks, New York became the first state to enact more liberal banking laws. *See generally* Note, *Foreign Banking in the United States*, 6 VAND. J. TRANSNAT'L L. 595 (1973).

The growth of foreign banks involves an increase in their number as well as their aggregate assets. Those banks which establish themselves in the United States are usually the largest in their own countries and rank among the largest in the world. The 99 foreign banks operating in the United States as of April 1977 included 65 of the 84 foreign banks which AMERICAN BANKER listed as the 100 largest commercial banks in the world. Wiegold, *Foreign Banks Here Practice Lessons Learned at Home — from Americans*, Aug. 8, 1977, at 13, col. 1.

[5] Professor Lees lists specific factors responsible for foreign banking expansion in the United States and summarizes the advantages available to foreign banks as a result of their United States presence. F. LEES, FOREIGN BANKING AND INVESTMENT IN THE UNITED STATES 17-18 (1976).

[6] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 102-03 (Letter from Arthur F. Burns to Ferdinand J. St. Germain (May 25, 1977)).

[7] Hackley, *Our Baffling Banking System* (pts. 1&2), 52 VA. L. REV. 565, 771 (1966).

complex interrelationships. The foreign bank entering the United States banking system must be aware of the distinctions between state and federal laws, the varying applications of federal laws to different classes of banks, and the division of federal regulatory authority among several agencies.[8] Some of the more "baffling" aspects of the domestic regulatory system are discussed below.

1. *Bank Charters.* All banks are chartered under either federal[9] or state law.[10] It has been alleged that the application of federal and state banking laws and regulations to the various types of commercial banks results in differing competitive advantages and disadvantages in each category.[11] Since every state has the power to legislate rules and regulations for its state-chartered banks, the restrictions placed on banks may vary significantly from state to state.[12]

All national banks are required to be members of the Federal Reserve System,[13] and all member banks, both national and state, are automatically covered by deposit insurance.[14] The Federal Deposit Insurance Act contains provisions which apply to both national and state banks obtaining federal deposit insurance. Member banks of the Federal Reserve System are subject to additional restrictions imposed by the Federal Reserve Act[15] and other federal laws.[16] In addition, the national banks are governed primarily by the provisions of the National Banking Act.[17]

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[8] *Id.*

[9] Banks chartered under federal law are known as "national banks." *Id.* at 566.

[10] Hackley classifies banks chartered under state law into three categories: "state member banks" are those state chartered banks which join the Federal Reserve System; "insured state banks" are those state chartered banks which obtain federal deposit insurance but do not join the Federal Reserve System; and "noninsured state banks" are those state chartered banks which neither obtain federal deposit insurance nor join the Federal Reserve System. *Id.*

[11] *Id.*

[12] *Id.* at 567. For a summary of state laws on foreign banking, see *Foreign Bank Act of 1975, Senate Hearings,* note 3 *supra,* at 18.

[13] The Board of Governors of the Federal Reserve System are authorized to regulate member banks, 12 U.S.C. § 221 *et seq.* (1970). The Federal Reserve Board determines general monetary, credit and operating policies of the Federal Reserve Sytem. It also establishes reserve requirements for member banks and regulates interest rates paid on savings deposits. Wermer, Frej, and Madway, *Redlining and Disinvestment: Causes, Consequences, and Proposed Remedies,* 10 CLEARING HOUSE REV. 501, 513 (1976).

[14] Hackley, *supra* note 7, at 566.

[15] Pub. L. No. 63-43, ch. 6, 38 Stat. 251 (codified, as amended, in various sections of 12 U.S.C. and 31 U.S.C. § 409 (1970)).

[16] The federal laws affecting banking include: Federal Deposit Insurance Corporation Act, 12 U.S.C. § 1811 *et seq.* (1970); Bank Holding Company Act, 12 U.S.C. § 1841 *et seq.* (1970); Edge Act, 12 U.S.C. § 611 *et seq.* (1970); Foreign Banking Acts, 12 U.S.C. § 601 *et seq.* (1970); Glass-Steagall Act, 12 U.S.C. § 347a, 347b, 412 (1970); McFadden Act, 12 U.S.C. §§ 36, 332 (1970); National Bank Acts, 12 U.S.C. § 21 *et seq.* (1970): Banking Act of 1933, ch. 89, 48 Stat. 162 (codified in scattered sections of 12, 15 & 39 U.S.C.); Banking Act of 1935, ch. 614, 49 Stat. 684 (codified in scattered sections of 11, 12, 15, 39 & 49 U.S.C.).

[17] Ch. 343, 18 Stat. 123 (codified in scattered sections of 5, 12, 18, 19, 28 & 31 U.S.C.).

2. *Federal Reserve Member Banks.* The Board of Governors of the Federal Reserve System regulates member banks.[18] Member banks must maintain a certain percentage of their demand and time deposits on reserve with their Federal Reserve Bank.[19] These reserves provide for a safer banking system, but earn no interest, thereby inhibiting the earning capacity of the member bank's funds. Member banks may utilize the discount window of the Federal Reserve as a temporary source of funds.[20]

3. *Federally Insured Banks.* The Federal Deposit Insurance Corporation (FDIC),[21] which establishes criteria for the insurance of bank deposits,[22] functions primarily as an insurance agency, and has regulatory power over non-member insured banks.[23] Among other things, the FDIC regulates bank mergers,[24] the establishment of branches,[25] and the payment of interest on deposits.[26]

4. *Bank Holding Companies.* According to the Bank Holding Company Act (BHCA),[27] a domestic or foreign entity must receive the approval of the FRB before becoming a bank holding company.[28] Thereafter, the bank holding company is subject to complete supervision by the FRB[29] and must receive its approval before acquiring direct or indirect ownership or control of any company.[30] Once within the regulation of the BHCA, foreign bank holding companies[31] are prohibited from engaging in non-banking activi-

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[18] Hackley, *supra* note 7, at 567.

[19] The Board of Governors of the Federal Reserve System are authorized to define demand and time deposits. 12 U.S.C. § 461 (1970). Crosse and Hempel describe required reserves as those portions of a bank's deposits in the form of cash on hand, deposits at Federal Reserve Banks, or demand balances due from specified banks which must be maintained at the Federal Reserve Bank of its district H. CROSSE & G. HEMPEL, MANAGEMENT POLICIES FOR COMMERCIAL BANKS 132 (1973).

[20] The extension of credit to member banks and the process of borrowing from the Federal Reserve Bank is referred to as using the discount window. P. NADLER, COMMERCIAL BANKING IN THE ECONOMY 35-37 (1973).

[21] 12 U.S.C. §§ 1811 et *seq.* (1970). The Federal Deposit Insurance Corporation (FDIC) was established under authority of section 8 of the Banking Act of 1933 and section 101 of the Banking Act of 1935 and provided a permanent plan of deposit insurance for the purpose of achieving sound, effective, and uninterrupted operation of the banking system. [1950] U. S. CODE CONG. SVC. 3765, 3766.

[22] The FDIC was originally created under § 12B of the Federal Reserve Act. In 1950 these provisions were withdrawn from the Federal Reserve Act and enacted, with further revisions, in a separate Federal Deposit Insurance Act. *See* 12 U.S.C. §§ 1811-31 (1970); Hackley, *supra* note 7, at 577 n. 74.

[23] Hackley, *supra* note 7, at 578.

[24] 12 U.S.C. § 1828(c) (Supp. V 1975).

[25] 12 U.S.C. § 1828(d) (1970).

[26] 12 U.S.C. § 1828(g) (Supp. V 1975).

[27] 12 U.S.C. §§ 1841-50 (1970).

[28] 12 U.S.C. § 1842(a), (b) (1970).

[29] 12 C.F.R. § 225.3 (1977).

[30] *Id., see also* Barnes, *The Fine Edge of Prohibition: Interstate and Foreign Banking in the United States,* 93 BANKING L. J. 911, 922 (1976).

[31] A foreign bank holding company "means a bank holding company, organized under the

ties, and subject to strict merger requirements.[32] Finally, multistate banking activities of foreign bank holding companies must be specifically authorized by state laws.[33]

5. *Investment Banking.* One of the purposes of the Banking Act of 1933[34] was to prohibit commercial banks from going into the investment banking business.[35] Section 21 of the Act, generally known as the Glass-Steagall Act,[36] takes a three-pronged approach.[37] First, it prohibits any

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laws of a foreign country, more than half of whose consolidated assets are located, or consolidated revenues derived, outside the United States." 12 C.F.R. § 225.4(g)(1)(iii) (1977).

[32] Edwards, *Regulation of Foreign Banking in the United States: International Reciprocity and Federal-State Conflicts,* 13 COLUM. J. TRANSNAT'L L. 251-52 (1974). While these are not the only restrictive aspects of the BHCA, Edwards cites these as particularly relevant to foreign banks. Title 12, Chapter II of the Code of Federal Regulations states that "A foreign bank holding company may: (i) Engage in direct activities of any kind outside the United States; (ii) Engage in direct activities in the United States that are incidental to its activities outside the United States; (iii) Own or control voting shares of any company that is not engaged, directly or indirectly, in any activities in the United States except as shall be incidental to the international or foreign business of such company; (iv) With the consent of the [FRB], own or control voting shares of any company principally engaged in the United States in financing or facilitating transactions in international or foreign commerce; (v) Own or control voting shares of any company, organized under the laws of a foreign country, that is engaged, directly or indirectly, in any activities in the United States if (a) such company is not a subsidiary of such bank holding company, (b) more than half of such company's consolidated assets and revenues are located and derived outside the United States, and (c) such company does not engage, directly or indirectly, in the business of underwriting, selling, or distributing securities in the United States; and (vi) Own or control voting shares of any company in a fiduciary capacity under circumstances which would entitle such shareholding to an exemption under section 4(c)(4) of the [BHCA] if the shares were held or acquired by a bank . . . ." 12 C.F.R. § 225.4(g)(2) (1977). A foreign bank holding company may apply to the FRB for a determination that other activities meet the conditions for an exemption under section 4(c)(9) of the BHCA. 12 C.F.R. § 225.4 (g)(3) (1977).

[33] Only two states presently permit acquisition of a local bank by an out-of-state bank holding company. Iowa prohibits out-of-state bank holding companies from acquiring Iowa banks except those holding companies (only one) having controlling interest in Iowa banks on January 1, 1971. IOWA CODE ANN. § 524.1805 (West 1977). Thus, Northwest Bancorporation can acquire local banks in Iowa. Iowa Independent Bankers v. Board of Governors of Federal Reserve System, 511 F.2d 1288 (D.C. Cir. 1975). Maine enacted legislation effective January 1, 1978, which authorizes acquisition of Maine banks by out-of-state holding companies provided that reciprocal privileges are extended to Maine banks. 9-B ME. REV. STAT. ANN. § 1013 (1977). *But see* Edwards, *supra* note 32, at 252, for California and New York exceptions.

[34] Ch. 89, 48 Stat. 162 (1933) (codified in scattered sections of 12 U.S.C. chs. 2, 3, and 6).

[35] Investment Co. Institute v. Camp, 401 U.S. 617, 629 (1971). "The Glass-Steagall Act reflected a determination that policies of competition, convenience, or expertise which might otherwise support the entry of commercial banks into the investment banking business were outweighed by the 'hazards' and 'financial dangers' that arise when commercial banks engage in the activities proscribed by the act." *Id.* at 630. The Supreme Court in effect said that the same hazards and abuses are present in 1970 and that the intent of the act is still alive. *Id.* at 639.

[36] Section 21 of the Banking Act of 1933 makes it unlawful to: (1) engage in the business of issuing, underwriting, selling, or distributing securities at the same time as engaging in the business of receiving deposits payable on demand; and (2) to engage in the business of

entity accepting deposits from simultaneously engaging in the securities business.[38] Secondly, it prohibits affiliation with organizations dealing in securities.[39] Thirdly, it prohibits interlocking directorates between member banks and such organizations.[40] Since a United States branch or agency of a foreign bank is not a "bank" for the purposes of these sections of the Act, a foreign bank may have both a United States branch or agency and a United States investment banking subsidiary, despite the prohibition against its direct involvement in the securities business.[41]

6. *International Interstate Banking (Edge Corporations).*[42] Edge Corporations are banking subsidiaries organized under the Federal Reserve Act[43] to conduct international banking and finance operations.[44] They may not engage in domestic banking.[45] Since Edge Corporations are federal corporations and are not governed by state banking regulations they can be formed in all 50 states.[46] Furthermore, the Edge Corporation is not defined as a "bank" under the BHCA;[47] therefore, it is not subject to Glass-Steagall restrictions on securities affiliates.[48] These Edge Corporations can also accept deposits incidental to its international transactions and in this

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receiving deposits payable on demand unless such business is incorporated or authorized by law to do so. 12 U.S.C. § 378(a)(1)(2) (1970).

[37] For a more complete discussion of the "Glass-Steagall Wall," see Lichtenstein, *Foreign Participation in United States Banking: Regulatory Myths and Realities*, 15 B. C. INDUS. & COMM. L. REV. 879, 891-94 (1974).

[38] 12 U.S.C. § 378(a)(1) (1970).

[39] 12 U.S.C. § 377 (1970).

[40] 12 U.S.C. § 78 (1970).

[41] Lichtenstein, *supra* note 37, at 894.

[42] Agreement corporations can also be included under this heading, but must agree to observe the same limitations and restrictions as those applicable to federally-chartered Edge Act subsidiaries. Solomon, *International Banking Competition and Cooperation*, 20 ANTITRUST BULL. 143, 144-45 (1975). Agreement corporations resulted from the state chartering of such institutions prior to the Edge Act legislation. *See* Lemmonds, note 44 *infra*, at 15. See Leimone, *Edge Act Corporations: An Added Dimension to Southeastern International Banking*, [1974] MONTHLY REV. 130 (Federal Reserve Bank of Atlanta) for a comparison of Agreement Corporations and Edge Corporations.

[43] 12 U.S.C. §§ 611-32 (1970).

[44] Lemmonds, *Edge Corporation: A Microcosm of International Banking Trends*, 59 MONTHLY REV. 15 (1973) (Federal Reserve Bank of Richmond).

[45] 12 C.F.R. § 211.1(b)(2) (1977). Edge activities are restricted to operations clearly related to international or foreign business.

[46] Lemmonds, *supra* note 44, at 15.

[47] 12 U.S.C. § 1841(c) (1970).

[48] Lichtenstein, *supra* note 37, at 975. The BHCA provides that no bank holding company shall retain ownership or control of a non-banking company unless authorized by the FRB. 12 U.S.C. § 1843(a) (1970). MacKenzie & MacKenzie state that since shares owned or controlled by any bank holding company subsidiary are deemed to be controlled by the bank holding company, 12 U.S.C. § 1841(g)(1970), the formation of an Edge Corporation by a subsidiary is the act of a bank holding company. MacKenzie & MacKenzie, *Penetration of the United States Market by a Foreign Bank*, 6 INT'L LAW. 876, 887-88 (1972).

sense can compete with local banks.[49]

7. *Domestic Interstate Banking.* Multistate branching restrictions of domestic banking operations are based on state legislation which prohibits an out-of-state bank from conducting domestic banking business.[50] National banks are also precluded under the McFadden Act[51] from crossing state lines to engage in domestic banking business.[52] Through the establishment of Edge Corporations, however, domestic banks can cross state lines for certain purposes.

B. *Organizational Options Available to Foreign Banks*

The type of organizational form chosen by the foreign bank can affect how it will be regulated by either state or federal authorities and will determine the banking activities the foreign bank may pursue. The options open to foreign banks are: (1) representative offices, (2) agencies, (3) branches,[53] (4) banking subsidiaries, and (5) investment subsidiaries.[54] The various powers, activities, and restrictions which distinguish the various organizational forms are set out in Figure 1.

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[49] Lichtenstein, *supra* note 37, at 901. Edge Corporations may engage in "such limited business in the United States as is usual in financing international commerce, including deposit facilities; loan, overdraft, advance acceptance, and other credit facilities; commercial letters of credit; foreign collections; purchase and sale of foreign exchange; remittance of funds abroad; purchase, sale, and custody of securities and acceptance for account of customers abroad; and foreign credit information." 12 C.F.R. § 211.7(a) (1977). Leimone indicates that Edge Corporations can accept demand and time deposits but not savings deposits as long as these deposits are in conjunction with their international business transactions. Leimone, *supra* note 42, at 133.

[50] Lichtenstein, *supra* note 37, at 889. The states have not authorized sister-state bank entry, much less entry by "foreigners."

[51] 12 U.S.C. § 36 (1970).

[52] First Nat'l Bank v. Dickinson, 396 U. S. 122, 130 (1969). In discussing the Banking Act of 1933, the Supreme Court noted that branch banking by national banks would be permissible only in those states the laws of which permit branch banking. First Nat'l Bank v. Walker, 385 U. S. 252, 259 (1966). Thus, Congress's intent is clearly to place national and state banks on a basis of competitive equality. *Id.* at 261.

Restricting the deposit gathering offices of any one bank to geographic areas such as state boundaries or the location of the initial office is a basic principle of United States banking regulation. Even if one state authorizes banks chartered by it to open branch offices outside of the state, reciprocal legislation in other states must be available before these branches can be established. Lichtenstein, *supra* note 37, at 895.

[53] Under New York law additional foreign bank branch activities include purchasing installment indebtedness, making secured advances repayable on demand to an amount not less than five thousand dollars, engaging in the safe deposit business, exercising certain limited fiduciary powers, and, if authorized by the Superintendent of Banks, operating a personal loan department. Edwards, *supra* note 32, at 243.

[54] For a detailed discussion of the organizational forms, see J. ZWICK, FOREIGN BANKING IN THE UNITED STATES, JOINT ECONOMIC COMMITTEE, PAPER NO. 9, 89th Cong., 2d Sess. 5-16 (1966).

FIGURE 1

Organizational Characteristic	Representative Office	Agency	Branch	Bank Subsidiary	Investment Company Subsidiary
1. Disseminate information about parent bank and promote good relations for parent bank	X	X	X	X	
2. Buy, sell, and collect bills of exchange		X	X	X	X
3. Issue letters of credit		X	X	X	
4. Transmit money abroad[55]		X	X	X	
5. Make Loans		X	X	X	X
6. Subject to lending limits[56]		X	X	X	X
7. Maintain credit balances		X	X	X	
8. Receive local deposits[57]			X	X	
9. Exercise fiduciary powers			X	X	
10. Presence conditional upon reciprocal treatment by foreign country[58]		X	X	X	
11. Requires prior federal approval under the BHCA				X	
12. Required to maintain reserves			X	X	
13. Constitutes a separate legal entity				X	
14. Federal deposit insurance required[59]			X	X	
15. Require American directors and shareholders				X	
16. Perform trust activities			X		
17. Depend on deposit expansion for growth			X		
18. Authorized to deal in securities[60]					X
19. Considered a "bank" under BHCA[61]				X	

[55] Except for Massachusetts, Oregon, and Washington. *Id.* at 35.

[56] The loan limit of agencies and branches is calculated on the basis of the capital position

As indicated in Figure 1, agencies, branches, and investment companies are not considered "banks" under the BHCA;[62] therefore, they are not eligible to receive federal deposit insurance. Additionally, investment companies can avoid the restrictions of the Glass-Steagall Act.[63] Agencies and branches have a greater loan capacity than subsidiaries.[64] Agencies cannot accept deposits[65] and, therefore, fractional reserve requirements are not applicable to them.[66]

At present, 14 states plus Washington, D.C., Guam, Puerto Rico, and the United States Virgin Islands have some form of foreign banking. Figure 2 below indicates the type of foreign banking conducted and the distribu-

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of the parent bank. The loan limit of a subsidiary is determined by the subsidiary's capital position; therefore, the subsidiary must generate substantial capital to allow it to make large loans. *Id.* at 5-6.

[57] MacKenzie & MacKenzie state that an agency may not be forbidden from holding funds deposited with its parent outside the state and repayable outside the state. Thus, a California agency could issue its parent bank's certificates of deposit to non-California corporations as long as the certificates are deliverable and repayable outside of California. MacKenzie & MacKenzie, *supra* note 48, at 884.

[58] A foreign banking corporation organized under the laws of a foreign country may be licensed in New York to maintain branches and receive deposits "if under the laws of such foreign country . . . a [New York] bank . . . may be authorized to maintain either a branch or agency." N.Y. BANKING LAW § 202(a) (McKinney 1971).

A foreign banking corporation in Illinois may not conduct banking business unless "under the laws of the country under which such foreign banking corporation was organized, [Illinois banks] may be authorized to maintain a banking office which may engage in a general banking business." ILL. ANN. STAT., ch. 16½, § 503 (Smith-Hurd 1977).

Georgia's International Bank Agency Act prevents the issuance of a license to a bank chartered in any country which does not allow banks from the United States to operate in that country. GA. CODE ANN. § 41A-3304(b) (rev. 1974).

[59] California law prohibits a foreign banking corporation from accepting deposits unless "it has been approved for Federal Deposit Insurance Corporation insurance . . ." CAL. FIN. CODE § 1756.1 (West 1968). As a result of this restriction, foreign bank branches in California cannot accept deposits because they are not eligible for FDIC insurance. The FDIC can only insure the deposits of banks (12 U.S.C. § 1811 (1970)) which are defined as banking institutions "incorporated under the laws of any State, any Territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands. . . . 12 U.S.C. § 1813 (a) (Supp. V 1975). Edwards states that because of their inability to accept deposits and because of the similarity of their powers to New York agencies, California branches are often called "operating agencies." Edwards, *supra* note 32, at 241, 243.

[60] N.Y. BANKING LAW § 508 (McKinney 1971). New York investment companies also have the power to establish branches under certain circumstances and to act as a depositary of public money of the United States.

[61] Branches, agencies, and investment companies are not "banks" within the meaning of section (2)(c) of the Bank Holding Company Act, 12 U.S.C. § 1841(c) (1970). Branches are not "organized under the laws of the United States," and neither agencies nor investment companies "accept deposits that the depositor has a legal right to withdraw on demand." Edwards, *supra* note 32, at 246 n. 47.

[62] *See* note 61 *supra*.

[63] Lichtenstein, *supra* note 37, at 975. *See* note 48 *supra*.

[64] *See* note 56 *supra*.

[65] Some agencies are allowed to accept foreign deposits. *See* note 59 *supra*.

[66] *See* note 53 *supra*, at 7.

FIGURE 2[68]

State	Subsidiaries or Affiliates	Branches[69]	Agencies	Representative Offices
CALIFORNIA	27		47	20
DISTRICT OF COLUMBIA	1			8
FLORIDA	1			3
GEORGIA	2		1	
GUAM				1
HAWAII	2		1	1
ILLINOIS	8	21		20
MARYLAND	1			
MASSACHUSETTS	4	1		
NEW YORK	63	65	42	110
OHIO				1
OREGON		4		
PENNSYLVANIA	2			1
PUERTO RICO	2	10		1
TEXAS	2			18
U.S. VIRGIN ISLANDS		7		
WASHINGTON		4		2
WISCONSIN	1			
TOTAL	116	112	91	186

tion within each state, territory, or possession. The remaining 36 states either expressly exclude foreign banks or do not mention them.[67]

III. PROBLEMS IN FEDERAL REGULATION OF FOREIGN BANKING

Any decision concerning federal regulation of foreign banking in the United States includes an evaluation of several conflicting viewpoints and interests. For example, the FRB is concerned about the grave implications of the ability of foreign banks to erode the FRB's control of monetary policy.[70] United States banks are concerned that foreign banks enjoy an unfair competitive advantage as a result of permissive federal regulation,[71] while foreign banks are concerned about the discriminatory effect of the

[67] Delaware, Texas, and Vermont prohibit foreign bank branches. Connecticut, Maryland, and New Jersey do not admit foreign bank offices in any form. The remaining states have enacted no statutory provisions which specifically refer to the establishment of foreign banks.

[68] Rolland, *Compilation of Foreign Bank Activities in United States American Banks*, AM. BANKER, Aug. 8, 1977, at 190-93. Note that the column heading "Subsidiaries or Affiliates" includes bank and investment company subsidiaries as shown in the "Bank Subsidiary" and "Investment Company Subsidiary" columns in Figure 1 as well as the branch offices of investment counselors and securities companies. *But see Int'l Banking Act of 1977, House Hearings, supra* note 1, at 95, Table 21, which lists 9 states, the United States Virgin Islands, and Puerto Rico as having some form of foreign banking.

[69] California branches are listed under agencies. *See* note 59 *supra*.

[70] J. ZWICK, *supra* note 54, at 26. *But see* Robertson and Phillips, *Optional Affiliation With the Federal Reserve Purposes is Consistent With Effective Monetary Policies, reprinted in Foreign Bank Act of 1975, Senate Hearings supra* note 3, at 393 (optional membership in the Federal Reserve System is not a contributory factor to monetary policy weakness).

[71] *Hearings on the "Discussion Principles" of the Financial Institutions and the Nation's*

regulatory system.[72] These and other conflicting concerns and interests are summarized below to assist in an evaluation of the IBA.

A. *Monetary Policy*

The FRB utilizes its regulatory control over member banks as an instrument in administering monetary policy.[73] However, agencies, branches, and state banks owned by foreign banks, which are not members of the Federal Reserve System, are not subject to any federal monetary policy promoted through member bank reserve requirements.[74] Despite this advantageous position, it is contended that foreign banking institutions do not currently present a threat to the effectiveness of United States domestic policy.[75]

B. *Discrimination Against Foreign Banks*

Foreign banks are not accorded equal treatment under United States laws.[76] For example, they are unable to obtain federal deposit insurance,[77] form Edge Corporations,[78] or exercise full banking powers in any of the 50 states.[79] Foreign banks attempting to establish national banks or Edge Corporations face restrictive citizenship requirements for directors and

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Economy (FINE) Study Before the Subcomm. on Financial Institutions Supervision, Regulation and Insurance of the House Comm. on Banking, Currency and Housing, 94th Cong., 1st and 2d Sess., pt. 3, 1794, 1796 (1975)(statement of Alexander McW. Wolfe, Jr.).

[72] Edwards, *supra* note 32, at 240.

[73] The FRB utilizes the discount rate and reserve requirements to exert monetary policy influence on member banks. However, the major monetary policy tool is open market operations which do not have exclusive application to member banks. The purchase and sale of government securities is an open market. Note, *The Federal Reserve System and the Formation of Monetary Policy*, 45 CIN. L. REV. 70, 73 (1976).

[74] State chartered banks and foreign bank agencies and branches may be subject to similar reserve requirements under state laws. However, the funds allowed to be held as reserves under state requirements are generally of an interest earning type and, therefore, state reserve requirements are not considered to be as restrictive. Edwards, *supra* note 32, at 267. *See* Klopstock, *Foreign Banks in the United States: Scope and Growth of Operations*, 55 MONTHLY REV. 140, 147 (1973) (Federal Reserve Bank of New York). *See also* F. LEES, *supra* note 5, at 64-66 and Auerback, *International Banking Institutions and the Understatement of the Money Supply*, 53 MONTHLY REV. 109-18 (1971) (Federal Reserve Bank of New York).

[75] *Compare* F. LEES, *supra* note 5, at 105, *with* INTERNATIONAL BANKING, *supra* note 1, at 736, 767-70, and Lucas, Jones, & Thurston, *Federal Funds and Repurchase Agreements*, 2 QUARTERLY REV. 33, 48 (Summer 1977) (Federal Reserve Bank of New York) which indicate that foreign banking presence in the United States substantially effects short-term capital flow and the balance-of-payments position.

[76] Edwards, *supra* note 32, at 261-65.

[77] Foreign branches (agencies and investment companies cannot receive deposits) are not "banks" as defined by 12 U.S.C. § 1813(a) and, therefore, cannot apply for FDIC insurance under 12 U.S.C. § 1815. Edwards, *supra* note 32, at 240-41; *see* note 59 *supra*.

[78] F. LEES, *supra* note 5, at 108-9. *See also* note 80 *infra*.

[79] As indicated in Figure 2, only a small number of states even allow foreign banking. *See* note 68 *supra*. *See also* Gilbert, *Foreign Banking in the United States*, 15 S.A.I.S. REV. 20, 23 (1971).

stockholders.[80] In short, foreign banks do not receive the same treatment that United States banks receive in foreign countries.[81]

C. *Unfair Competitive Advantages*

Although United States banks claim that foreign banks are afforded certain opportunities that work to the detriment of domestic banks,[82] it is doubtful whether these competitive advantages have significantly affected the banking industry. In the area of multistate international banking, national banks have the advantage since foreign banks are restricted to the number of states in which they are allowed to operate.[83] Foreign banks can transact international business only in those states which expressly authorize their presence. National banks, on the other hand, can engage in international banking in any state through an Edge Corporation. However, foreign banks have the advantage in the area of multistate domestic banking business.[84] Foreign banks can conduct domestic banking business in any and all of those states authorizing their presence, while United States banks cannot cross state lines to engage in domestic banking. Also, foreign banks are allowed to have security affiliates,[85] while the Glass-Steagall Act

[80] Every director of a national bank must be a citizen of the United States. 12 U.S.C. § 72 (1970). All directors of an Edge Corporation must likewise be citizens of the United States. 12 U.S.C. § 614 (1970). A majority of the shares of capital stock of any Edge Corporation shall at all times be held or owned by citizens of the United States. 12 U.S.C. § 619 (1970). Consequently, difficulties are encountered in obtaining suitable citizens to serve as directors, and the home office cannot control the operation. J. ZWICK, *supra* note 54, at 5.

[81] United States bank's foreign offices are generally permitted the same banking powers as all other banks in that country. However, foreign banks entering, or attempting to enter, the United States banking system are faced with different and generally more restrictive regulations than United States banks, federal or state. The generally accepted meaning of reciprocity is that foreign banks should be given the same banking powers and should be placed under the same regulatory constraints as are American banks in the United States, although they should not be permitted activities permissible in their homelands, but prohibited by the United States banking laws. Edwards, *supra* note 32, at 257-61. *See Foreign Bank Act of 1975, Senate Hearings,* note 3 *supra,* at 226-31 for a survey of foreign regulation of United States banks.

[82] American bankers allege unfair treatment because foreign banks are allowed securities affiliates and because foreign banks are allowed to function on a multistate basis. Edwards, *supra* note 32, at 262. Domestic banks also allege competitive disadvantages in the areas of costs of funds, arbitrage, and reserve requirements. F. LEES, *supra* note 5, at 64.

[83] F. LEES, *supra* note 5. *See* Figure 2, at note 68 *supra.*

[84] F. LEES, *supra* note 5, at 108-09. This advantage is somewhat lessened by the restrictions placed on these foreign banks. For example, Georgia only allows foreign banks to operate in the agency form; Illinois only allows foreign banks to locate in the Chicago loop area; and California, in effect, only allows bank branches to operate as agencies. Also note that generally foreign banks are only interested in locating in the principal banking centers and not in establishing a nationwide branch system. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 648 (Swiss Bank's Policy Position on International Banking Act of 1976).

[85] Since foreign bank agencies, branches, and investment companies are not considered banks (*see* note 61 *supra*), foreign banks can have an operational presence in the United States in one or more of these forms in addition to a security affiliate. However, the number and effect of foreign bank security affiliates are alleged to be too insignificant to justify federal

prohibits such investment opportunities for domestic banks.[86]

State and federal reserve requirements are generally similar in amount, but different in form.[87] Those assets required by the FRB to be held in federal reserve banks produce no income and represent "frozen assets" that contribute nothing to bank earnings. In contrast, state nonmember banks can apply a wide list of assets to satisfy state reserve requirements and can thereby generate income from the required reserves with routine money management.[88] While domestic banks may choose not to be member banks should they decide that the restrictive measures outweigh the advantages of membership, foreign bank agencies, branches, and investment companies have no such alternative since they may not become member banks.[89] Foreign banks are also not eligible for federal deposit insurance.[90] While this may seem to offer a cost advantage,[91] it also is a disadvantage in that it restricts operating flexibility where state law allows foreign banks to accept deposits.[92] Finally, foreign banks are in an excellent position to engage in arbitrage operations between the principal money and credit markets during times of "tight money."[93] Since arbitrage is generally based on very small price discrepancies, such cost advantages resulting from more favorable reserve requirements become very significant in these transactions.[94]

D. *Regional Development Interests*

Foreign banking has grown substantially in regional centers[95] as these centers recognize the potential economic growth that can be derived from

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legislation. Schneider, *Legislation to Limit Foreign Banking Here Would Hurt, Not Help the U.S.*, AM. BANKER, Aug. 8, 1977, at 62, col. 4. *cf. Foreign Bank Regulation in the U.S.A.: The Federal Reserve Proposals*, 125 BANKER 47 (1975) [hereinafter cited as *Foreign Bank Regulation]* which refers to three foreign owned and nine domestically owned investment companies in New York.

[86] In limiting the securities activities in which banks can participate, the Glass-Steagall Act precluded high-risk, high-gain potential investments. Thus, while it ensured that the banking industry remains a low risk industry, it also reduced the profit potential of banking investments. Edwards, *supra* note 32, at 263.

[87] *See* note 73 *supra.*

[88] F. LEES, *supra* note 5, at 65.

[89] *See* note 61 *supra.*

[90] *See* note 77 *supra.*

[91] The federal deposit insurance premium assessment is equivalent to approximately three percent of pretax net income. F. LEES, *supra* note 5, at 65.

[92] Branches in California can only accept deposits if they have FDIC insurance. *See* note 59 *supra.*

[93] "Arbitrage" can be defined as the "simultaneous purchase and sale of the same or equivalent security, commodity contract, insurance, or foreign exchange on the same or different markets in order to profit from price discrepancies." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 110 (1968).

[94] F. LEES, *supra* note 5, at 66-71. *See also* Klopstock, note 74 *supra*, at 46-47. Less restrictive reserve requirements allow more funds for arbitrage operations.

[95] Rolland, *Foreign Bank Presence Grows Substantially in New York, California and New Regional Centers*, AM. BANKER, Aug. 8, 1977, at 1, col. 1. *See* Leimone, *The Spread of Interna-*

international trade and investment.[96] Due to this correlation between foreign banking and economic growth,[97] restrictions placed upon foreign banking operations will favor some regional areas over others.[98]

E. *International Considerations*

The reciprocity provisions[99] of several state statutes may be inconsistent with present United States treaty obligations.[100] This potential for conflict between state legislation on foreign banking and the United States treaty commitments indicates a need for federal participation in negotiations with foreign banks.[101] In addition, the discriminatory treatment afforded foreigns banks in the United States could prompt retaliatory legislation by foreign countries. Fear of foreign retaliation against restrictive United States banking practices prompted the more liberal banking legislation in the late 1950's.[102] Such retaliation today would be devastating to the major United States banks, since foreign banking operations have been a major source of their income in recent years.[103]

F. *Jurisdictional Issues*

Legislators are concerned with the jurisdictional problems related to foreign banking. The directors of foreign banks are foreign citizens living

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tional Banking: A Regional View, [1971] MONTHLY REV. 142 (Federal Reserve Bank of Atlanta).

[96] Dempsey, *Legal and Economic Incentives For Foreign Direct Investment in the Southeastern United States*, 9 VAND. J. TRANSNAT'L L. 247, 250 (1976). *See* Baer, *Expansion of Miami Edge Act Corporations*, [1977] ECONOMIC REV. 112 (Federal Reserve Bank of Atlanta); Baer and Garlow, *International Banking in the Sixth District*, [1977] ECONOMIC REV. 127 (Federal Reserve Bank of Atlanta).

[97] *Georgia Knocks at the World's Door*, ATLANTA, Jan. 1974, at 57; Adcock, *Atlanta's New International Connection*, SOUTH, May/June 1977, at 50; McWolfe, *Florida Gains Importance as Major Foreign Banking Center*, AM. BANKER, Oct. 17, 1977, at 10, col. 1.

[98] Schneider, *supra* note 85, at 141, col. 1. *See also* 122 CONG. REC. H7,949 (daily ed. July 29, 1976) (remarks by Rep. Rousselot and Rep. Tsongas).

[99] *See* note 58 *supra*.

[100] The United States is obligated under numerous treaties of Friendship, Commerce and Navigation (FCNs) to conform to standards of national treatment. National treatment within the context of the FCNs means to accord to companies of those countries signing the treaty the same treatment accorded "to companies created or organized in other states, territories, and possessions of the United States of America." *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 237 (Memorandum From Paul Boeker to Committee on Foreign Investment in the United States (March 23, 1976)).

At the House Hearings of the International Banking Act of 1977 Paul H. Boeker testified in favor of the bill. However, he indicated that certain sections of the bill may impinge upon the United States obligations under the FCN treaties. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 275-80. *See also* Lichtenstein, *supra* note 37, at 885-86.

[101] Note, *supra* note 4, at 615.

[102] *See* note 4 *supra*.

[103] Barnes, *supra* note 30, at 938-39. Unfair curbs on foreign banks may lead to retaliation by foreign countries. Dowleng, *Curbs on Foreign Banks Seen Leading to Retaliation*, AM. BANKER, July 14, 1977, at 1, col. 1. In response to congressional legislation to restrict foreign banks to a single state, United States banks could be confined to one city or country within the Common Market. Such a limitation would have a devastating impact on United States

in a foreign country and may not be subject to United States jurisdiction. Personnel of foreign banks can easily remain, or be transferred, outside United States jurisdictional limits. Additionally, essential records may be difficult, if not impossible, to reach if they are maintained in foreign countries. Finally, in the event of insolvency of a foreign bank's operation, assets may not be subject to creditors' claims, nor may foreign depositors be willing to subrogate their claims to United States regulatory agencies.[104] Thus, a regulatory scheme with neither *in personam* nor *in rem* jurisdiction over the parties or the assets would be ineffective.

IV. EVALUATION OF THE INTERNATIONAL BANKING ACT OF 1978

The International Banking Act of 1978 would provide federal regulation of foreign bank participation in domestic financial markets.[105] The purpose of this Act is to give foreign banking institutions the same rights, duties, and privileges as domestic banks, while subjecting them to the same limitations, restictions, and conditions.[106] This section examines the IBA in the context of the problems highlighted in the previous section and evaluates its effectiveness in accomplishing its stated purpose.

A. *FRB Controls*

The rapid growth of foreign banking institutions in the United States resulted in the FRB's original proposal to federally regulate foreign banks.[107] The IBA proposes a comprehensive regulatory system to control the foreign bank's impact on the nation's money and credit markets while maintaining the principle of "nondiscrimination" or "national treatment."[108]

1. *Defining the Foreign Bank*

"Foreign bank" has been defined as encompassing all foreign banking

banking in Europe. *Foreign Bank Regulation, supra* note 85, at 57. Schneider states that United States banks abroad are more vulnerable to restrictive legislation than foreign banks in the United States with an estimated 125 United States banks having aggregate foreign assets of over $150 billion. Schneider, *supra* note 85. *See also* Leimone, *Foreign Branches Add to Growth*, [1973] MONTHLY REV. 112 (Federal Reserve Bank of Atlanta). Mr. Paul Fabre stated that the practical effect of such restrictive legislation would be "to give free rein to U.S. banks and securities firms to compete very strongly in Europe in all areas." *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 371.

[104] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 561-62 (statement of George Le Maistre).

[105] Comm. Print, *supra* note 2, at 1.

[106] *Id.* at 46.

[107] 122 CONG. REC. H7,936-7 (daily ed. July 20, 1976) (remarks by Rep. Moakley). *See also* F. LEES, *supra* note 5, at 113-15. The FRB has consistently maintained the position that Congress should enact legislation which provides for the regulation and supervision of foreign banks operating in the United States. More specifically, the FRB has recommended that such litigation establish a national framework in which comparable foreign and domestic banking institutions are governed by the same type of banking and monetary regulations. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 101 (Letter from Arthur F. Burns to Ferdinand St. Germain (May 25, 1977)).

[108] *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 46 (statement of George

activities conducted in the United States.[109] The focus of the definition has now shifted from actually engaging in banking activity to an institution's "power" to engage in banking business,[110] thus, eliminating the incentive for organizing shell banking corporations abroad which do business solely in the United States.[111] Literally construed, the proposed definition would subject a foreign institution to IBA regulation where its activities are "usual in connection with the business of banking" in its homeland, regardless of what the scope of the usual business of banking is in the United States.[112]

W. Mitchell). For a definition of national treatment, *see* note 100 *supra*.

[109] The term "foreign bank" has undergone several definitional changes since the original FRB proposal. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 280, § 18(a)(2). Section 18(a)(2) of that proposal defined "foreign bank" in terms of being "principally engaged in the banking business outside the United States." *Id.* The definition was revised to "principally conducts its banking business outside the United States" in the International Banking Act of 1976, *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 91, § 1(b)(7), and that definition was carried through to the initial proposal of the International Banking Act of 1977, *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 4, § 1(b)(7).

However, the FRB has identified two main problems with that definition:

1) it excludes a foreign owned bank which principally conducts its business in this country, and

2) it is not clear whether the "principally conducts business" test is subject to a one-time interpretation or is to be continuously updated.

At the time, the FRB recommended that authority be granted to the FRB or the Comptroller of the Currency to change the scope of the definition so as to prevent evasion of the Act. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 114 (statement of Stephen S. Gardner). The Institute of Foreign Banks expressed no objection to the redefinition of the term but opposed the discretionary sweep of the definition proposed by the FRB. *Id.* at 507 (statement of Institute of Foreign Bankers).

Another change in the scope of the definition has also been evident in the progression of bills. While not in the original Foreign Bank Act of 1975, the phrase "subsidiary, as that term is defined in the Bank Holding Company Act" was inserted into the definition of "foreign bank" proposed in § 1(b)(7) of the *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 91. This phrase was continued in the initial proposal of the International Banking Act of 1977, but has been deleted in the latest Comm. Print, *supra* note 2, at 3, § 1(b)(7). This deletion excluded from the definition of "foreign bank" any foreign subsidiary not "organized under the laws of the United States, [or] any State of the United States . . . which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans." 12 U.S.C. § 1841(c) (1970). Although under previous definitions New York's authorized investment companies could have avoided the effect of this Act by refraining from accepting deposits and from the business of making commercial loans, under the revised definition the IBA brings the New York investment companies within its scope.

[110] *Compare Int'l Banking Act of 1977, House Hearings, supra* note 1, at 5, § 1(b)(7) *with* Comm. Print, *supra* note 2, at 3, § 1(b)(7).

[111] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 115.

[112] The exact phrasing of the bill states "engage in banking activities usual in connection with the business of banking in the countries where such foreign institutions are organized or operating." Comm. Print, *supra* note 2, at 3, § 1(b)(7). Note that while investment banking is usual in connection with the business of banking in Europe, it is legislatively excluded from the allowable scope of banking activities in the United States. *See* note 36 *supra*.

2. *Citizenship Requirements*

The citizenship requirements for national banks[113] would be amended to allow the Comptroller of the Currency in his discretion to allow "not more than a minority of the total number of directors" to be foreign citizens.[114] The citizenship requirements for Edge Corporations[115] would also be amended to delete the requirement that all directors shall be citizens of the United States.[116] It also would allow 50% or more of the shares of capital stock to be held by foreign interests, subject to FRB approval.[117] These revisions would permit foreign banks to become member banks able to form Edge Corporations in any state in the United States.[118] Previous proposals which granted the FRB discretionary powers to waive both the reserve requirements for Edge Corporations' authorized deposits and the limits on outstanding liabilities are omitted from the proposed IBA, in accordance with the goal of national treatment of foreign banking institutions.[119]

3. *Federal Branches and Agencies*

The IBA would authorize the incorporation of federal branches and agencies subject to the approval of the Comptroller of the Currency. Thus, for the first time, both branches and agencies would be treated in international banking legislation.[120] The IBA would establish a dual system of foreign banks, distinguishing state branches, agencies, and commercial lending companies from federal branches and agencies. The former would

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[113] 12 U.S.C. § 72 (1970).

[114] Comm. Print, *supra* note 2, at 4.

[115] 12 U.S.C. § 614 (1970).

[116] Comm. Print, *supra* note 2, at 5.

[117] Comm. Print, *supra* note 2, at 5-6.

[118] As previously mentioned, foreign banks may not form Edge Corporations and therefore, are restricted in the number of states in which they can operate. Lichtenstein has suggested that problems of unfair competition could be resolved by offering the Edge Corporation option to foreign banks on an exclusionary basis. That is, if the Edge Corporation option was chosen, the foreign bank could not also utilize branches and subsidiaries on a multistate basis. These provisions have followed this suggestion fairly closely. Lichtenstein, *supra* note 37, at 975. According to Leimone, however, citizenship requirements for stockholders and directors do not apply to Agreement Corporations which operate under state charters while submitting to FRB regulation. This suggests the possibility that foreign banks can form Agreement Corporations to engage in international banking activities. Leimone, *supra* note 42, at 132.

[119] The initial proposal in § 3(b)-(c) of both the International Banking Act of 1977 and the International Banking Act of 1976, provided that the Edge Corporation minimum reserve requirements, which are the same as those for member banks, be eliminated with the approval of the FRB to insure competitive equality between branches and agencies of foreign banks and Edge Corporations. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 116.

[120] Comm. Print, *supra* note 2, at 7, §§ 4-5. In the initial FRB proposal, the Foreign Bank Act of 1975 only applied to foreign bank branches. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 280, § 18. The scope of the proposed federal regulation was expanded in 1976 to include foreign branches and agencies. *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 95, § 4. The FRB in the hearings on the International Banking Act of 1977 recom-

be subject to state regulatory authority, while the latter would be "conducted with the same rights and privileges as a national bank at the same location" and "subject to all the same duties, restrictions, penalties, liabilities, conditions, and limitations that would apply to a national bank doing business at the same location."[121] Foreign banks seeking to establish an initial presence in the United States would be allowed to establish a federal branch or agency in any state in which the establishment of a branch or agency is not prohibited by state law. Foreign banks with existing branches and agencies in only one state would have to determine whether to convert all branches and agencies to federal branches and agencies or retain their status as state branches and agencies.[122] Foreign banks with existing branches and agencies in more than one state would have to designate a home state and determine whether to convert branches and

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mended that federal agencies not be subjected to the capital equivalency requirements since they are precluded from receiving deposits. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 118 (statement of Stephen S. Gardner). The current IBA does not follow the FRB's recommendation and failed to exclude federal agencies from capital equivalency requirements as had been done in the International Banking Act of 1976 and the initial proposal of the International Banking Act of 1977.

[121] Comm. Print, *supra* note 2, at 7, § 4. Two notable exceptions to national bank treatment are that federal branches and agencies are not required to become member branches and that federal agencies are not required to become federally insured banks.

This language, as it concerns the deposit acceptance capability of federal branches, may be subject to two interpretations. First, it may mean that, since Edge Corporations are the only means whereby a national bank can engage in interstate banking, federal branches would be subject to the same rights, privileges, and restrictions as an Edge Corporation. Under this interpretation, federal branches could only accept deposits incidental to international transactions and could *not* accept domestic deposits. A broader interpretation, however, would allow federal branches to exercise the same banking powers as a national bank *whose home office* was located at that location. Such powers would include the acceptance of domestic deposits and would place the federal branch in a position to compete for local deposits. The IBA would check this power because section 4(a) provides that the state may prohibit the establishment of a foreign bank branch, and section 5(a) provides that the state must expressly permit the establishment of a federal branch. Under this broader interpretation, therefore, the state would still control the receipt of deposits from the general public.

The first interpretation would apply solely to the foreign bank choosing to operate a federal branch outside its home state as provided for in section 5 of the IBA. The broader interpretation would apply solely to the foreign bank seeking to establish an initial presence in the United States through a federal branch. These two interpretations could result in federal branches having different deposit taking capabilities. Furthermore, those foreign banks not currently established in the United States would be able to offer a broader range of services which would penalize those foreign banks already present in the United States.

[122] The IBA prohibits a foreign bank from maintaining both a federal branch and agency in the same state, Comm. Print, *supra* note 2, at 9, § 4(e), and both a federal branch or agency and a state branch or agency in the same state. *Id.* at 7, § 4(a). A strict construction of the IBA, therefore, mandates that a foreign bank wishing to maintain multiple branches or agencies in a single state can only do so if they are all federal branches or all federal agencies. As listed in Figure 2, New York is the only state to have both foreign bank branches and foreign bank agencies. Although eight banks have more than one branch in the city, there are no New York banks which have both branches and agencies in the state. Rolland, *supra* note 68, at 190, col. 1. Under New York law, a foreign bank cannot operate both an agency and a branch in New York. N.Y. BANKING LAWS § 202(d) (McKinney 1971).

agencies to federal branches and agencies or remain within the state regulatory system.[123]

The IBA would also require that assets be held in each state in which a federal branch or agency is established.[124] The general purpose of this asset requirement is to ensure that, in the event of insolvency, there will be sufficient assets in the state to satisfy the claims of United States creditors and depositors.[125]

4. *Reserve Requirements*

The IBA would place federal branches and agencies under the same reserve requirements as member banks, but would grant discretionary authority to the FRB to waive the prescribed reserve requirements in order to maintain vigorous and fair competition between member banks and federal branches and agencies.[126] Federal branches and agencies would be subjected to reserve requirements only if the total worldwide consolidated bank assets of their parent bank were in excess of $1 billion.[127] Such a requirement follows the recommendation of the FRB[128] but is not in keeping with the goal of national treatment of foreign banks. Previous proposals pertaining to reserve requirements had included all foreign bank branches, agencies, and commercial lending companies, but foreign banking interests protested the discriminatory nature of such a proposal.[129]

The IBA would also grant federal branches and agencies access to the clearing, discount, and advance facilities of the Federal Reserve System specifying that due regard be given to the federal branch or agency's account balances maintained as reserves.[130] Such discretionary authority can operate to both discourage competitive inequality and to encourage foreign bank participation and national treatment.

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[123] *See* text at notes 76-81.

[124] Comm. Print, *supra* note 2, at 11, § 4(g)(4).

[125] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 119.

[126] Comm. Print., *supra* note 2, at 34, § 7(a)(1).

[127] *Id.* at 35, § 7(a)(2). The Foreign Bank Act of 1975 established mandatory membership in the Federal Reserve System if its parent bank had total worldwide bank assets of $500 million. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 258, § 3(3). The International Banking Act of 1976 imposed a similar mandate except that the threshhold amount for mandatory membership was raised to $1 billion. *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 106, § 7(a)(2).

[128] The FRB maintains that since the foreign banks in the United States have the same characteristics as the large domestic United States banks, which are all federal reserve members, the foreign banks should be members for reasons of equity (Letter from Stephen S. Gardner to Dr. Wolfgang Jahn (June 2, 1977) *reprinted in Int'l Banking Act of 1977, House Hearings, supra* note 1, at 135).

[129] The Institute of Foreign Bankers maintained that denying federal reserve membership choice to foreign bank agencies and branches cannot be viewed abroad as anything but discrimination unless the arbitrary size distinctions are applied to domestic banks as well as to foreign banks. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 481-94.

[130] Comm. Print, *supra* note 2, at 36, § 7(b).

5. *Monetary Policy*

For a number of years the FRB has been attempting to include nonmember depository institutions within its reserve setting authority, claiming that it needs such authority to perform its role in setting monetary policy more efficiently.[131] Considerable comment and criticism have been directed at the inappropriateness of such authority-extending attempts. No similar mandatory membership or reserve requirements are imposed on domestic banks.[132]

B. *Multistate Banking Operations*

The IBA would offer a foreign bank three alternatives for operating outside its "home state:"[133] (1) as a state branch, agency, or commercial lending company, (2) as a federal branch or agency, or (3) as a bank acquired under section 3 of the BHCA. If the foreign bank chose to operate as a state branch, agency, or commercial lending company, it would have to be "approved by the regulatory authority of the state in which . . . [it] is to be operated."[134] This alternative would ensure minimum disruption of existing foreign bank operations, since all foreign branches and agencies currently operate under the auspices of state law. It would also obviate the necessity of a grandfather clause, since foreign banks presently can have state branches, agencies, and commercial lending companies in more than

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[131] *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 396-98 (statement of John B. Olin).

[132] The New York Clearing House Association argues that since no similar mandatory membership or reserve requirements are imposed on domestic banks it is difficult to support the premise that such requirements are necessary to assure foreign bank compliance with United States monetary policies. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 301 (statement of John F. Lee). The Conference of State Bank Supervisors also states that the FRB has not demonstrated that optional affiliation with the system by our domestic commercial banks has impeded the application of its monetary policy controls nor that foreign banks operating in the United States have had a similar effect. *Id.* at 318 (statement of William E. Whitesell).

[133] According to § 5(b) of the IBA, the home state of foreign bank—

(1) which has no branch or subsidiary bank in the United States, but which has an agency or commercial lending company in one or more States, is whichever of such States is determined by election of the bank, or, in default of such election, by the Board of Governors of the Federal Reserve System.

(2) which has a branch or subsidiary bank in one State only, is that State.

(3) which has a branch or subsidiary bank in more than one State, is whichever of such State is determined by election of the bank, or, in default of such election, by the Board of Governors of the Federal Reserve System.

Comm. Print, *supra* note 2, at 16, § 5(b).

[134] Previous drafts and proposals had prohibited foreign branching outside the home state unless domestic banks could likewise branch. The Foreign Bank Act of 1975 made foreign banks subject to the same intrastate branching restrictions as national banks, *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 286, § 18(i), and prohibited the acquisition of additional banks located outside the state. *Id.* at 258, § 3(2). The International Banking Act of 1976 prohibited interstate operations by federal or state branches unless a national bank was entitled to the same branching privileges. *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 101, § 5(a). The International Banking Act of 1977 as introduced to the House

one state, subject to state regulation.[135]

If a foreign bank chose to operate a federal branch or agency, it would have to be "expressly permitted by the state in which it is to be operated."[136] In operating a federal branch or agency across state lines, a foreign bank would be subject to restrictions similar to those imposed upon a national bank,[137] which is prohibited from crossing state lines,[138] except in the form of an Edge Corporation. However, while a national bank can establish an Edge Corporation without the approval of banking authorities in the state in which it is to be operated, the IBA would require foreign banks to obtain express permission from the state in which it plans to operate a federal branch or agency.[139] Such a requirement is inconsistent with the goal of national treatment of foreign banks.[140]

Finally, if a foreign bank chose to acquire a bank under section 3 of the BHCA, it would have to be a "bank holding company the operation of whose banking subsidiaries were principally conducted in the foreign bank's home state."[141] The FRB must approve and the state statutes must specifically authorize such an accquisition.[142] Since only two states[143] allow such acquisitions, this restriction is tantamount to prohibition.[144] An addi-

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of Representatives had the same restriction on interstate banking as the International Banking Act of 1976, *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 14, § 5(a).

[135] *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 253, § 3, *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 101, § 5(a)-(b), and *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 14, § 5(a)-(b). Each included a statement that prohibited multistate operation of foreign branches or agencies that did not comply with the provisions of the specific act and that were not established prior to a specified date. The intent of these grandfather clauses was to avoid unfairly causing existing foreign banking branches and agencies to close after they had been legally established in good faith under existing laws. The IBA obviates the necessity for a grandfather clause in multistate operations by allowing foreign banks to continue to maintain their state branches, agencies, and commercial lending companies in more than one state, subject to state regulation.

[136] Comm. Print, *supra* note 2, at 15, § 5(a)(2).

[137] *See* note 121 *supra* and accompanying text.

[138] National banks can establish branches only where state law would authorize state banks to establish branches. 12 U.S.C. § 36 (1970). *See* note 33 *supra*.

[139] State regulatory authorities may, therefore, expressly deny permission to federal branches and agencies even though that state allows the formation of state foreign bank branches and agencies. The reason for this difference lies in the type of banking business in which the foreign bank may engage. State branches and agencies may generally compete in both domestic and international banking business while the federal branch or agency may only compete in international banking business. Thus, a state wishing to avoid foreign banking competition in its domestic market may only allow federal branch or agency operations.

[140] Since the Institute of Foreign Bankers maintains that it is a fundamental principle of its interstate branching practice not to enter a state that does not want foreign banking presence, the effect of such restriction should not be severe. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 509-10 (statement of the Institute of Foreign Bankers).

[141] Comm. Print, *supra* note 2, at 15, § 5(a)(3).

[142] 12 U.S.C. § 1842 (1970).

[143] *See* note 33 *supra*.

[144] At least this restriction gives interested states the option to amend their statutes so as to allow such interstate acquisitions rather than federally legislating a matter considered to

tional consideration of the multistate branching provisions is that a foreign bank would be allowed to acquire a subsidiary bank only if the operations of the acquiring bank holding company's subsidiaries were "principally conducted" in the foreign bank's home state.[145]

This selection of alternatives presents an interesting problem. If the foreign bank chose to remain within the state regulatory system, then no change would occur, since under present law it cannot operate in the state without the approval of the state regulatory authority. If, however, the foreign bank chose to convert to federal branches or agencies, a conflict could occur. Since a federal branch or agency would have to be "expressly permitted by the State in which it is to be operated,"[146] the state might be able to prevent the foreign bank from converting to, or even forming, a federal branch or agency simply by refusing to expressly permit its operation. This dilemma might be avoided by inferring permission from state statutes authorizing existing foreign branch or agency activity, even though the states might legislatively deny such an inference by requiring express permission. In either case each state would have direct authority to approve the operation of a federal branch or agency in that state. This situation differs from Edge Corporations, which require approval only from federal authorities.

Several prohibitions may prevent a foreign bank from converting to federal branches. A foreign bank would not be able to establish a federal branch or agency in any state in which it were operating a branch or agency pursuant to state law.[147] In addition, no foreign bank would be able to maintain both a federal branch and a federal agency in the same state.[148] For example, in New York, which is the only state having both foreign branches and foreign agencies,[149] three banks have more than one branch,[150] and no New York bank has both a branch and an agency.[151] Therefore, a foreign bank operating more than one branch or agency in New York would have to convert them to either federal branches or agencies if it chose that alternative.

C. *Federal Deposit Insurance*

The effectiveness of the FDIC in protecting the financial stability of insured banks stems not only from a system of insuring deposits but also

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be a state's prerogative. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 586 (statement of Robert Bloom).

[145] The term "principally conducted" is subject to the same criticism the FRB made of this wording when used to define "foreign bank." *See* text at note 109 *supra*.

[146] *Id.* at 15, § 5(a)(2).

[147] *Id.* at 7, § 4(a).

[148] Comm. Print, *supra* note 2, at 9, § 4(e).

[149] *See* Figure 2, at note 68 *supra*.

[150] Barclays Group, Standard and Chartered Banking Group Limited, and Swiss Bank Corporation each have two branches in New York. *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 180-82 (statement of John B. Olin). *See* note 122 *supra*.

[151] Under New York Law, a foreign bank cannot operate both an agency and a branch in New York. N.Y. BANKING LAW § 202(d) (McKinney 1971).

from regulatory restrictions designed to lower the risk of bankruptcy.[152] Unlike previous proposals,[153] which dealt only with the aspect of depository insurance, the IBA seeks to bring foreign bank branches fully within the regulatory jurisdiction of the FDIC.[154] The major consideration for such an effort is that such jurisdiction cannot be extended to the foreign bank's activities abroad but must be applied to the foreign bank's branches in the United States.[155]

The IBA would make federal deposit insurance mandatory for foreign bank branches and thereby provide regulatory control by the FDIC.[156] Foreign banking interests maintain that this requirement would discriminate against them in favor of other banks operating in the United States.[157]

The IBA would define "insured deposits" so as to exclude from coverage foreign bank branch deposits not payable in the United States and deposits meeting the criteria prescribed by the FDIC.[158] No such distinction would

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[152] These regulations include capital requirements, liquidity requirements, loan standards, reporting procedures, and entry restrictions. Edwards, *supra* note 32, at 266.

[153] The Foreign Bank Act of 1975 provided that within 90 days of its enactment the FDIC was to submit to Congress a proposal for amending the Federal Deposit Insurance Act to include within the coverage of such act, branches and agencies of foreign banks. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 279, § 17. The International Banking Act of 1976 deleted foreign bank agencies from consideration and specified that a branch accepting deposits must maintain a surety bond or a pledge of assets with the FDIC. *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 104, § 6. This wording was carried over to the initial proposal of the International Banking Act of 1977 without change. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 17, § 6.

[154] Comm. Print, *supra* note 2, at 18, § 6(b).

[155] Edwards, *supra* note 32, at 266.

[156] Existing branches are allowed a one year grace period to become insured banks. Comm. Print, *supra* note 2, at 18, § 6(b).

[157] The European Economic Committee's Banking Federation considers this requirement to be discriminatory, since FDIC insurance is optional for the majority of American banks. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 348 (statement of European Economic Community Banking Federation). The Institute of Foreign Bankers submitted testimony that federal deposit insurance is not necessary for foreign banks since they do not engage in a significant amount of domestic retail banking business. *Id.* at 517 (statement of Institute of Foreign Bankers). This contention, however, is somewhat misleading. Since 43 states require federal deposit insurance for state chartered banks (New York specifically exempts foreign banks) and less than 1% all banks in the United States are not insured, the practical effect of this requirement is equitable. Interview with Jane D'Arista, Staff, House Comm. on Banking, Finance and Urban Affairs, (Mar. 17, 1978).

[158] The IBA would revise 12 U.S.C. § 1813(m) (Supp. V 1975) to specify that foreign bank branch deposits are insurable if they were

> Payable in the United States to—(i) an individual who is a citizen or resident of the United States, (ii) a partnership, corporation, trust, or other legally cognizable entity created under the laws of the United States or any State and having its principle place of business within the United States or any State, or (iii) an individual, partnership, corporation, trust or other legally cognizable entity which is determined by the Board [FDIC] in accordance with its regulation to have such business or financial relationships in the United States as to make the insurance of such deposit consistent with the purposes of this Act . . . .

Comm. Print, *supra* note 2, at 19, § 6(c)(4). The FDIC is also granted discretion to establish additional criteria as necessary or appropriate to maintain the viability of the Act.

be made for domestic insured banks.[159] The definition of "insured branch"[160] in the IBA differs from the definition of "insured bank"[161] under the Federal Deposit Insurance Act in that the IBA would consider a foreign bank branch to be an insured branch when "any deposits" were insured, whereas the Federal Deposit Insurance Act requires that *all* deposits be insured to obtain this classification.[162]

The IBA would require a surety bond or pledge of assets "to provide protection to the deposit insurance fund against the risks . . . of a foreign bank whose activities, assets, and personnel are in large part outside the jurisdiction of the United States."[163] The FDIC stated that to require a security bond or pledge of assets as the sole guarantee of deposit liability is both onerous and impractical,[164] especially in light of the other regulatory restrictions placed on insured banks. The FDIC proposed a more equitable solution that would utilize a modified form of the surety bond and pledge of assets to compensate for the additional[165] risks to which the FDIC would be subjected.[166] It is not clear whether or not the intent of the IBA is to comply with the FDIC proposal which more closely adheres to the goal of national treatment of foreign banks.[167] If not, this provision would be discriminatory since it would not be applied to domestic insured banks. Furthermore, under the IBA, the FDIC would retain the right to exercise its judgment in imposing additional requirements of larger bonds and more assets "without notice or opportunity for hearing."[168] If the foreign bank failed to comply, the FDIC would be given authority to apply for injunction against *any* branch of that bank within the jurisdiction of United States

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[159] 12 U.S.C. § 1813(m) (Supp. V 1975).

[160] "The term 'insured branch' means a branch of a foreign bank any deposits in which are insured in accordance with the provisions of this Act." Comm. Print, *supra* note 2, at 21, § 6(c)(6).

[161] "The term 'insured bank' means any bank the deposits of which are insured in accordance with the provisions of this Chapter [the FDIC]." 12 U.S.C. § 1813(h) (1970).

[162] The IBA definition could also be interpreted to include all deposits but no clarification is offered in the bill. A further explanation could be that the wording was an attempt to recognize that not all deposits in a foreign bank branch could be insured.

[163] Comm. Print, *supra* note 2, at 21, § 6(c)(7).

[164] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 564 (statement of George A. LeMaistre).

[165] The risks involved in international operations are both greater than and different from the risks with which banks are normally familiar. Reimpell, *International Lending Holds Extra Risks Which Could Be Made Less Hazardous*, AM. BANKER, Oct. 19, 1977, at 26, col. 1. *But see* Ruckdeschel, *Risk in Foreign and Domestic Lending Activities of U.S. Banks*, 10 COLUM. J. WORLD BUS. 50 (1975).

[166] This modified form of surety bond and pledge of assets is combined with the regular deposit insurance coverage of domestic insured banks and would put foreign banks as nearly as possible on an equal basis. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 565-66.

[167] If this is the intent of the IBA, then for clarification the word "additional" should be inserted before the word "risk" so that the statement of purpose would read as follows "to provide protection to the deposit insurance fund against the *additional* risks entailed . . . ." (emphasis added).

[168] Comm. Print, *supra* note 2, at 27, § 6(c)(7).

courts[169] to have the necessary assets delivered to the FDIC. The IBA would also grant discretionary authority to the FDIC to adjust the assessments of insured branches "to provide equitable treatment for domestic and foreign banks."[170]

Additionally, the IBA would give the FDIC a right to a cause of action against "a foreign bank or any officer, director, employee, or agent thereof" for acts or practices outside the United States by simply alleging a belief that "such act or practice . . . is likely to be a cause of or carried on in connection with or in furtherance of" activities which are unsafe or unsound and jeopardize the insurance risk assumed by the FDIC.[171]The penalty for such practice would be the termination of the insured status of the foreign bank or branch.[172]

Venue and jurisdiction would be provided at the situs of the branch or bank affected.[173] The IBA would also provide the FDIC with power to take action to reopen or avert the closing of an insured branch of a foreign bank.[174] Another provision would provide that merger transactions involving a foreign bank are excluded from the regulatory authority of the FDIC "if no party to the transaction is principally engaged in business in the United States."[175] This wording is also used to exclude dealings between a foreign bank having an insured branch and any affiliate thereof.[176] As previously mentioned, however, the exact meaning of "principally engaged" has not yet been determined.[177]

Thus, the IBA proposes to extensively revise the current Federal Deposit Insurance Act, making foreign bank branches eligible for federal deposit insurance. However, the numerous restrictions imposed on foreign bank branches do not achieve the goal of nondiscriminatory or national treatment; nevertheless, they may provide an insurance structure which would be as equitable as possible considering the additional risks and jurisdictional conflicts inherent in the regulation of foreign banks.

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[169] *Id.* In evaluating the discriminatory nature of such treatment, the nature of the risks involved must also be considered. The risks associated with international financing are in part a function of the economic and political environment of the foreign country(s) involved and can generally be said to increase with geographic distance. An additional risk is that resulting from fluctuations in exchange rates. Where such factors can greatly increase the risk to any financial venture, it is reasonable to provide the FDIC with some discretionary authority so as to adjust their exposure to this risk. Reimpell, *supra* note 165.

[170] Comm. Print, *supra* note 2, at 26, § 6(c)(11).

[171] *Id.* § 6(c)(15).

[172] The FDIC can protect its assumed risk, therefore, without having to seek punishment or judgment against a person or entity outside the court's jurisdiction.

[173] Comm. Print, *supra* note 2, at 28, § 6(c)(15).

[174] *Id.* at 31, § 6(c)(25).

[175] *Id.* at 32, § 6(c)(26).

[176] *Id.* § 6(c)(29).

[177] *See* note 109 *supra.*

D. *Non-Banking Activities*

Under section 8, the IBA would attempt to bring foreign banks' non-banking activities within the regulation of the BHCA of 1956, as amended in 1970:[178]

> Any foreign bank that maintains a branch or agency [inclusive of federal branches and agencies] in a State, any foreign bank or foreign company controlling a foreign bank that controls a commercial lending company organized under State law, and any company of which any foreign bank or company [referred to above] is a subsidiary shall be subject to the provisions of the BHCA.[179]

According to the European Economic Community Banking Federation,[180] section 8 of the IBA would effectively preclude certain foreign banks or non-banking firms from establishing or maintaining their presence in the United States.[181] The drastic effect of this provision stems from the fact that the European approach to banking is so markedly different from that of the United States.[182] Congress has previously recognized this radically divergent view of foreign banking structures in its discussion of and amendments to the BHCA.[183] Allowing these foreign bank activities, to some extent, however, would negate the purpose behind the BHCA.[184]

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[178] 12 U.S.C. § 1841-50 (1970). See Lichtenstein, *supra* note 37, at 917-43, for a detailed discussion of foreign bank regulation under the Bank Holding Company Act.

[179] Comm. Print, *supra* note 2, at 40, § 8(a). This is almost identical to the provision of the *Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 110, § 8(a), and is the exact wording of the initial draft of the *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 23, § 8(a). However, the approach of the original FRB proposal, Foreign Bank Act of 1975, was completely different. It would have made any foreign bank exercising control over a branch or agency of the foreign bank, which was established and operating under the laws of the United States, a holding company. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 253, § 2.

[180] The European Economic Community Banking Federation represents the bankers associations of each of the nine member-countries of the European Common Market.

[181] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 352 (statement of European Economic Community Banking Federation). The BHCA prohibits bank holding companies from engaging in nonbanking activities. 12 U.S.C. § 1843 (1970). The EEC Banking Federation's interpretation stems from this proscription. Thus, according to the EEC Banking Federation a foreign bank, which retains ownership in United States subsidiaries, engaged in nonbanking activities cannot establish a banking presence in the United States, even if the nonbanking subsidiary in the United States is owned by the holding company which controls the foreign bank. Likewise, where a foreign bank controls a nonbanking firm which has subsidiaries in the United States, that foreign bank cannot establish or maintain a banking presence in the United States.

[182] F. LEES, *supra* note 5, at 80. *See also* Lichtenstein, *supra* note 37, at 917-43.

[183] Lichtenstein, *supra* note 37, at 917-43.

[184] The purpose of the Bank Holding Company Act was to provide adequate safeguards against undue concentration of control of banking activities. Because of the importance of the banking system to the national economy, the dangers accompanying monopoly in this field are particularly undesirable in view of the significant part played by banking in our present national economy. [1956] U.S. CODE CONG. & AD. NEWS 2482.

Therefore, attempts to regulate the banking industry would have to consider this dilemma and balance the goals of national treatment against the stability of the United States banking system and national economy.

The IBA has taken the approach recommended by the FRB,[185] which would amend the BHCA[186] to allow foreign bank holding companies to retain and acquire non-banking companies principally engaged in business outside the United States.[187] Three exceptions would be made to this statutory exemption: (1) the foreign holding company may not engage in securities activities in the United States which would not be allowed if it were a United States holding company,[188] (2) the exemption may not be used to avoid the restrictions of section 4(c)(8) of the BHCA,[189] and (3) affiliates may not be offered more favorable credit terms than other borrowers.[190] A further amendment to this provision explicitly states that for purposes of the BHCA a bank holding company would be "principally engaged" in business in the United States if its principal banking subsidiary were in the United States.[191] According to the FRB, the general purpose of this provision would be to ensure that the United States banking approach would not be forced on foreign banking operations which are primarily outside the United States.[192]

Also included within the non-banking restrictions of the IBA would be the foreign bank's securities activities in the United States. The same international conflict of banking approaches is also applicable to securities activities, but in this area the United States regulatory attitude is not as amenable to exceptions as in the area of other non-banking activities. In

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[185] The FRB made the same recommendation in testimony at the hearings on both the International Banking Act of 1976 (*Int'l Banking Act of 1976, Senate Hearings, supra* note 3, at 38-41), and the International Banking Act of 1977 (*Int'l Banking Act of 1977, House Hearings, supra* note 1, at 129-32).

[186] 12 U.S.C. § 1841 (1970).

[187] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 131. (statement of Stephen S. Gardner).

[188] This exception prevents foreign holding companies from avoiding the restrictions of the Glass-Steagall Act. *Id.*

[189] Section 4(c)(8) of the Bank Holding Company Act is codified in 12 U.S.C. § 1843(c)(8) (1970). *Id.*

[190] This exception prevents foreign banks' United States affiliates from having an unfair competitive advantage over the United States' competitors. *Id.* The Institute of Foreign Bankers maintains that this principle is followed in practice, but protests that the administrative burden of monitoring comparable credit terms is impracticable and too great for the FRB. *Id.* at 505 (statement of Institute of Foreign Bankers).

[191] Comm. Print, *supra* note 2, at 44, § 8(e). "This prevents large United States banking organizations from ever being able to use the exemption." *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 132 (statement of Stephen S. Gardner).

[192] Since any companies principally engaged in business within the United States are included within the requirements of the BHCA, foreign banks or their affiliates operating principally in the United States are prevented from any significant competitive advantages and those foreign banks wishing only to establish minimal United States operations are not discouraged from doing so. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 132.

fact, the Institute of Foreign Bankers maintains that section 8 seems primarily derived from concerns that the Glass-Steagall Act does not prevent foreign banks from having both banking and securities affiliates in the United States.[193] Foreign banks' opposition to this particular regulatory restraint seems to be more vigorous than to any other provision of the IBA.[194] Again, this opposition stems from the differences in the two systems, since many European banks derive a considerable share of their business from securities, trading, underwriting, and portfolio management.[195] In European countries securities activities are an inherent function of commercial banking activities.[196] Despite the difference in banking approaches and despite the possible dissolution of foreign owned securities firms, the IBA restrictions would not prevent those affected foreign banks from continuing to provide the same service to their customers. Indeed, loss of service to their customers seems to be the major reason for their opposition to the restraint on securities activities.[197] The IBA would only preclude operating directly in the market. The broker option is still available and can be continued in the same volume with the same exchanges with which they deal at present. Thus, the service could still be provided to their customers. This restriction does not seem as violative of national treatment as the foreign bankers claim because domestic banks are precluded from such activities as well, and the foreign banks have alternative means for providing the same service.

Non-banking activities (except securities activities) which were commenced or acquired prior to December 3, 1974[198] would be allowed to continue their current activities indefinitely.[199] Non-banking activities acquired after that date would have to be divested by December 31, 1985.

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[193] *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 520. (statement of Institute of Foreign Bankers).

[194] Miller, *Foreign Banking in the United States: Growth Sparks Legislative Controversy,* EUROPEAN COMMUNITY, Nov.-Dec. 1977, at 11, 14.

[195] F. LEES, *supra* note 5, at 80.

[196] Such a restriction would cause foreign bank owned securities affiliates to close and preclude European banks from doing business in the United States securities markets. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 344 (statement of European Economic Community Banking Federation).

[197] The European Economic Community Banking Federation maintains that their securities issues are tailored for the United States market and are not marketable in Europe. Furthermore, they maintain that the United States secondary market is essential to place such issues. *Id.* at 345 (statement of European Economic Community Banking Federation).

[198] This was the date of the grandfather clause as originally proposed in the hearings before the Subcommittee on Financial Institutions and which has been carried forward throughout all subsequent proposals. *Foreign Bank Act of 1975, Senate Hearings, supra* note 3, at 253, § 2.

[199] The FRB may terminate such grandfathered activities if it finds "that such action is necessary to prevent undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices in the United States." Comm. Print, *supra* note 2, at 41, § 8(c).

However, different grandfather rules would apply for the securities activities of foreign banks. All securities activities would have to be divested by December 31, 1985, the grandfather date. A foreign bank's securities' affiliates would be permitted, however, to continue to engage in the business "of underwriting, distributing, or otherwise buying or selling stocks, bonds and other securities in the United States . . . to the extent not prohibited for national banks by . . . 12 U.S.C. § 24 . . . as long as . . . [these activities] are confined to jurisdictions other than the United States."[200] Both the Institute of Foreign Bankers and the Conference of State Bank Supervisors contend that securities activities regulations would be more appropriately considered under amendments to the Glass-Steagall Act.[201]

The IBA also explicitly states that for the purposes of the Bank Holding Company Act of 1956, as amended in 1970, nothing in section 8 would be construed to define a branch or agency of a foreign bank or a commercial lending company controlled by a foreign bank as a "bank."[202] This exclusion is somewhat confusing in that foreign bank agencies or commercial lending companies of a foreign bank had not heretofore been considered "banks" since neither form "can accept deposits that the depositor has a legal right to withdraw on demand."[203] However, where foreign bank branches had not heretofore been considered "banks" within the meaning of section 2(c) of the BHCA because they were not "organized under the laws of the United States," the IBA would provide that federal branches would be incorporated under the laws of the United States and could accept deposits tha might be withdrawn on demand. Absent this provision federal branches would be considered a "bank" under the BHCA. Since "branch" is inclusive of "federal branch," this provision apparently intends to exclude federal branches. Of course federal agencies would still be precluded because of their inability to accept deposits.

E. *Conclusion*

The IBA provides an opportunity for the United States to establish a national regulatory system which equitably manages foreign banking interests. It includes a number of provisions to facilitate the accomplishment of its goal of a national treatment of foreign banks. The creation of a dual

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[200] *Id.* Thus, as long as the foreign bank's security affiliate confines itself to countries outside the United States it can continue its affiliation.

[201] They contend that section 8 should be deleted from the IBA at least until the Subcommittee on Securities of the Senate Committee on Banking, Housing and Urban Affairs completes its current review of the Glass-Steagall Act. *Int'l Banking Act of 1977, House Hearings, supra* note 1, at 323, (statement of Conference of State Bank Supervisors). *Id.* at 521 (statement of the Institute of Foreign Bankers). Apparently, however, this study does not examine the investment banking problems raised by the IBA. *Id.* at 215. *See also* Edwards & Zwick, *Activities and Regulatory Issues: Foreign Banks in the United States*, 10 COLUM. J. WORLD BUS. 58, 66 (1975).

[202] Comm. Print, *supra* note 2, at 43, § 8(d).

[203] Edwards, *supra* note 32, at 246.

system of foreign banking, in effect separating the state and federally chartered foreign banks, attempts to provide foreign banks with an equal opportunity to engage in the various facets of banking. The ambiguity of the deposit taking powers of federal branches, however, needs to be clarified.

The section 8 restrictions on foreign banks' securities activities have met with much opposition, causing a growing fear of foreign retaliation against United States banking activities abroad. This provision would be more properly considered as an amendment to the Glass-Steagall Act.

The relaxation of restrictive citizenship requirements and the attempt to provide federal deposit insurance for foreign banks are indicative of a more equitable attitude toward foreign banks. There remains, however, a considerable gap between the potential effect of the IBA and its stated purpose of national treatment, as evidenced by the restrictions on the establishment and multistate branching of federal branches and agencies. As this gap closes it will become more apparent whether this "separate but equal" policy toward foreign banks will be effective.

Patrick F. McMahon

As this Note goes to print, several amendments to the IBA were adopted on February 28, 1978, by the full House Committee on Banking, Finance, and Urban Affairs. An amendment by Representative St. Germain (Rhode Island) revised section 5, Interstate Banking Operations. Using identical wording to the International Banking Act of 1977, this amendment would subject federal branches and agencies to the same interstate branching restrictions as national banks. As in the International Banking Act of 1977, this restriction would preclude interstate branching by foreign banks via federal branches and agencies. State branches, agencies, and commercial lending companies could be operated outside the foreign bank's home state only if (1) the statute laws of the state in which the branch or agency would be located expressly authorize such operation and (2) such operation were approved by that state's regulatory authority. This provision would be somewhat more restrictive than the IBA in that it would require express statutory authorization in addition to approval by the state's regulatory authority. However, while existing foreign bank activities outside the home state would not be terminated, further interstate branching would depend upon express statutory approval and might require some states to amend their statutes. The proposed amendment, would reinsert a grandfather clause permitting the continued existence of interstate activities commenced prior to May 1, 1976.

Representative St. Germain has also proposed an amendment to section 7, Authority of the Federal Reserve System, in response to which, Representative Brown (Michigan) has offered a substitute proposal. Representatives St. Germain and Brown both propose that state branches, agencies, and commercial lending companies, whose parent bank meets the threshold amount of $1 billion in total worldwide consolidated assets may be subjected by the FRB to the same reserve requirements as federal branches and agencies after consultation with state bank supervisory authorities. While Representative Brown would add that such requirements should be imposed in cooperation with state regulatory authorities, both proposals would give the FRB sole authority to determine whether these reserve requirements should be imposed. This provision would be a clear infringement of current state regulatory powers. Both proposals would also provide that examination reports made by state regulatory authorities should be submitted to the FRB upon request. Additionally, Representative St. Germain

proposed that subject to the authority of the FRB any limitation or restriction based on capital stock and surplus and applicable to a state member bank should be applicable to the state branch, agency, or commercial lending company of a foreign bank. Representative Brown's substitute proposal was adopted.

Representative Hanley (New York) makes perhaps the most important amendment revising the IBA. Under Representative Hanley's amendment to section 8, Nonbanking Activities, the restriction on foreign bank's securities activities in the United States would be deleted. Because of tremendous opposition to these restrictions and because of the potential for foreign bank retaliation if these restrictions were enacted, it is doubtful the IBA could be passed without Representative Hanley's amendment. Representative Grassley (Iowa) also offered an amendment to revise section 9, Guidelines for Foreign Bank Operations, which would enable the Secretary of the Treasury to take into account any retaliatory treatment by foreign governments in response to the IBA.