

Chapter 8

FDIC Insurance and Regulation of U.S. Branches of Foreign Banks

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§ 8:1 Overview

A foreign bank wishing to engage in retail deposit-taking activities in the United States may no longer do so through a branch office insured by the Federal Deposit Insurance Corporation (FDIC).¹ Instead, the foreign bank must now organize or acquire an insured U.S. bank subsidiary.² The relatively few foreign bank branches that were FDIC-insured on December 19, 1991, have been grandfathered and may continue to engage in a full range of deposit-taking activities in the United States—including retail deposit taking—so long as they remain FDIC-insured.³ However, all other U.S. branches of foreign banks must confine their deposit taking in the United States to activities not requiring FDIC

[Section 8:1]

¹During the economic and banking crisis of the Depression, Congress created the FDIC through the enactment of the Banking Act of 1933, Pub. L. No. 66, 48 Stat. 162, 168 (1933) (codified as amended in scattered sections of 12 U.S.C.A.). Through Section 8 of the Banking Act of 1933, Congress added Section 12(B) to the Federal Reserve Act (FRA). Section 12(B), as amended, was subsequently withdrawn from the FRA and designated the “Federal Deposit Insurance Act” (FDI Act) (codified at 12 U.S.C.A. §§ 1811 to 1834b). Congress intended the FDIC to promote the safety and soundness of the banking system, enhance public confidence in the banking system, prevent runs on banks, safeguard deposits, and prevent further bank holidays, such as the bank holidays that occurred in March of 1933. *See, e.g.*, 77 Cong. Rec. 81, 82, 489, 3727, 3728, 4240, 4241 (1933) (underlying goals of Congress in establishing federal deposit insurance). *See also* Doherty v. United States, 94 F.2d 495, 497 (8th Cir. 1938), *aff’d* 18 F. Supp. 793 (D. Neb. 1937), *cert. denied*, 303 U.S. 658, 58 S. Ct. 763, 82 L. Ed. 1117 (1938) (insurance scheme created to promote stability of U.S. banking system).

²12 U.S.C.A. § 3104(c). Federal law requires FDIC insurance for all national banks, state banks that are members of the Federal Reserve System, and all domestically chartered, full-service commercial banks (including state nonmember banks) that are subsidiaries of bank holding companies. *See* 12 U.S.C.A. §§ 222, 1814(b), 1842(e). However, most limited-purpose banking and trust companies (including credit-card banks, Edge Act corporations, and the like) are not required to have FDIC insurance. *See* 12 U.S.C.A. § 1842(e). In addition, almost all states require FDIC insurance for state-chartered commercial banks as a condition of receiving a charter, either by statute, regulation, or as a matter of administrative policy or practice. *See, e.g.*, N.Y. Banking Law § 32.

³12 U.S.C.A. § 1815(a).

insurance protection,⁴ also known as “wholesale” deposit-taking activities.

This chapter discusses the historical background of FDIC insurance of U.S. branches of foreign banks in Section 8:2. In Section 8:3, the current regulations of both the FDIC and the Comptroller of the Currency (OCC or Comptroller) defining “domestic retail deposit activities requiring deposit insurance protection” are explained. These regulations define the permissible “wholesale” deposit-taking activities of all nongrandfathered branches of foreign banks and thus set forth the limits upon the activities of those branches. Finally, the FDIC’s regulations governing the relatively small number of insured U.S. branches of foreign banks that were grandfathered on December 19, 1991, are covered briefly in Section 8:4.

§ 8:2 Historical background

Before enactment of the International Banking Act of 1978 (IBA),⁵ U.S. banking offices of foreign banks were not subject to legislation or regulation at the federal level. Consequently, foreign bank branches were neither required by federal law to obtain, nor eligible under federal law to receive, FDIC insurance. As a result, in order to obtain FDIC insurance for U.S. deposit-taking activities before 1978, a foreign bank had to organize or acquire an insured U.S. bank. Notwithstanding objections from the FDIC,⁶ the IBA—in order to ensure “parity of treatment be-

⁴12 U.S.C.A. § 3104(c)(1).

[Section 8:2]

⁵Pub. L. No. 95-369, 92 Stat. 607 (1978) (codified at 12 U.S.C.A. §§ 3101 to 3108 and scattered other sections of 12 U.S.C.A.).

⁶On June 21, 1978, George A. LeMaistre, then-Chairman of the FDIC, testified during hearings on the IBA that the agency “had serious reservations about the necessity and desirability of making deposit insurance coverage available for domestic branches of foreign banks. These reservations arise from a concern that insufficient legal and regulatory controls could be placed on branch operations that are not legally separate from those of the parent bank.” International Banking Act of 1978: Hearings on H.R. 10899 Before the Subcomm. on Financial Institutions of the Senate Committee on Banking, Housing & Urban Affairs, 95th Cong., 2d Sess. 93, 103-04 (1978) (statement of George A. LeMaistre, Chairman, Federal Deposit Insurance Corporation); *see also* International Banking Act of 1977: Hearings on H.R. 7325 Before the Subcomm. on Financial Institutions, Supervision, Regulation and Insurance of the House Committee on Banking, Finance, and Urban Affairs, 95th Cong., 1st Sess. 546 (1977) (statement of George A. LeMaistre, Chairman, Federal Deposit Insurance Corporation) (substantially similar statement).

tween foreign and domestic banks in like circumstances”⁷—required foreign bank branches that were not “wholesale” in nature to maintain FDIC insurance in most circumstances.⁸ Under the IBA, FDIC insurance became statutorily mandated for foreign branches accepting deposits of less than the standard maximum deposit insurance amount (SMDIA), which was \$100,000 at the time of the IBA’s enactment, unless the branch was determined by order or regulation to be “not engaged in domestic retail deposit activities requiring deposit insurance protection.”⁹ The SMDIA currently is \$250,000 in light of amendments under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) to the FDI Act.¹⁰

The FDIC used its regulatory authority to expand substantially the IBA’s “wholesale” exemption to include various types of deposits of less than the SMDIA that could be accepted by a state-chartered branch without triggering the requirement of FDIC insurance.¹¹ Most significantly, the FDIC’s regulations applied the IBA’s SMDIA threshold only to the “initial deposit” transaction between the branch and its depositor.¹² As a result, all subsequent deposit transactions with that depositor were also “wholesale” and could take place without further amount restric-

⁷The IBA implemented this principle to provide in general more comparable treatment at the federal legislative and regulatory level for foreign bank operations in the United States (a policy of “national treatment”). *See* S. Rep. No. 95-1073, at 2 (1978), reprinted in 1978 U.S.C.C.A.N. 1421, 1422.

⁸IBA § 6, 92 Stat. 607, 614. The insurance requirement was imposed on each branch prospectively. The threshold amount for “wholesale” deposits was generally accepted to be \$100,000.

⁹IBA § 6, 92 Stat. 607, 614. Statutory authority and responsibility for making the determination was given to the Comptroller for federally licensed branches, and to the FDIC for state-licensed branches. IBA § 6(a), (b). In the case of state-licensed branches, the requirement applied only in those states where state-chartered banks were required to be FDIC-insured. IBA § 6(b). The FDIC, however, interpreted this condition to be satisfied whenever state law, regulation, or policy required state-chartered banks to have FDIC or state deposit insurance when accepting deposits from the general public. *See* 44 Fed. Reg. 40,056, 40,057 n.3 (1979) (language in the preamble accompanying promulgation of the FDIC’s final regulations implementing the IBA); *see also* 12 C.F.R. § 346.4(b). As a result, the requirement of FDIC insurance applied in virtually all states to state-licensed branches of foreign banks engaged in “domestic retail deposit activities requiring deposit insurance protection.”

¹⁰*See* Dodd-Frank Act § 335, 124 Stat. 1376, 1540.

¹¹*See* the FDIC’s final rule implementing the IBA, 44 Fed. Reg. 40,056 (1979) (current version at 12 C.F.R. Pt. 347).

¹²*See* 12 C.F.R. §§ 347.213 (uninsured branches), 347.202(m) (definition of initial deposit).

tions and without regard to account balances. The FDIC also determined that certain other types of deposit accounts could be established with “initial deposits” of less than the SMDIA because they did not require deposit insurance protection.¹³

As a result of the FDIC’s regulatory expansion of the “wholesale” exemption, foreign bank branches were able to avoid the IBA’s requirement of FDIC insurance by limiting their deposit-taking activities.¹⁴ In fact, during the time FDIC insurance was available to all foreign bank branches,¹⁵ most elected to remain uninsured.¹⁶ Uninsured status enabled these branches oriented to “wholesale” commercial banking to avoid numerous burdensome regulations and statutes that were applicable to insured branches as well as the FDIC’s deposit insurance assessments and asset maintenance requirements.¹⁷

¹³The categories of permissible deposit relationships that can be established by uninsured branches of foreign banks with initial deposits of less than the SMDIA are currently set forth at 12 C.F.R. § 347.215. See § 8:3 for a discussion of the applicability of the FDIC’s current regulations to uninsured U.S. branches of foreign banks and for a summary of the Comptroller’s regulations governing retail deposit activity by uninsured federal branches of foreign banks.

¹⁴The Comptroller initially incorporated by reference the FDIC’s regulations governing permissible uninsured deposit activities into its regulations for federal branches. See 44 Fed. Reg. 65,379, 65,383, 65,385 (1979) (final regulations of the Comptroller implementing the IBA). The Comptroller’s regulations governing the operation of foreign banks in the United States through federal branches and agencies have subsequently been completely revised and no longer simply reference the FDIC’s standards for permissible uninsured deposit activities. See 61 Fed. Reg. 19524 (1996).

¹⁵See 12 C.F.R. § 346.8.

¹⁶Only 27 foreign banks maintained one or more insured U.S. branches as of December 19, 1991. See *Insured U.S. Branches of Foreign Banks* (revised January 15, 1992), compiled by the FDIC; see also *Subsidiary Requirement Study*, app. C (Implications for the Deposit Insurance System (Factor 2)) (Study prepared by the Secretary of the Treasury and the Board of Governors of the Federal Reserve System (FRB), in consultation with the Comptroller, the FDIC, and the Attorney General of the United States) (submitted on December 18, 1992, by the Secretary of the Treasury to the Chairmen of the Banking Committees of the respective Houses of Congress) (“Subsidiary Requirement Study”).

Historically, U.S. branches of foreign banks did not aspire, as a business matter, to compete with FDIC-insured banks in attracting retail deposits in the United States even when FDIC insurance was available to such branches. The relatively rare exceptions to this rule have generally involved foreign bank branches located in U.S. communities having high concentrations of ethnicity related to the home country of the foreign bank maintaining the branch office. See *Subsidiary Requirement Study*, app. C, at 2.

¹⁷FDIC-insured status historically triggered the applicability to insured branches of a number of U.S. laws generally applicable to “insured banks,” to

The deposit insurance structure established by the IBA remained in place for foreign bank branches for a little more than a decade. However, in the wake of the highly public problems of two foreign banks, Banca Nazionale del Lavoro and Bank of Credit and Commerce International (BCCI), Congress, in 1991, implemented a new, stricter regulatory scheme for foreign banks operating in the United States.¹⁸ Among its other provisions, the Foreign Bank Supervision Enhancement Act of 1991 (FBSEA)¹⁹ generally prohibited foreign banks from accepting or maintaining in the United States “deposit accounts having balances of less than the SMDIA” other than through an insured U.S. bank subsidiary.²⁰ Branches of foreign banks that had been FDIC-insured on December 19, 1991, were grandfathered from this prohibition.²¹

The language of the prohibition in the FBSEA was not

which uninsured branches of foreign banks were not otherwise subject. These included the Community Reinvestment Act (CRA), 12 U.S.C.A. §§ 2901 to 2906, federal law restrictions on loans to insiders, 12 U.S.C.A. § 1828(j)(2), and, in the past, various other consumer-oriented laws and regulations.

¹⁸See Misback, *The Foreign Bank Supervision Enhancement Act of 1991*, 79 Fed. Res. Bull. 1 (Jan. 1993).

¹⁹The FBSEA was enacted as Title II of the Federal Deposit Insurance Corporation Improvement Act of 1991, Pub. L. No. 102-242, 105 Stat. 2236 (1991) (codified at 12 U.S.C.A. § 3104(c)).

²⁰FBSEA § 214(a), 105 Stat. 2236, 2303 to 2304 (codified at 12 U.S.C.A. § 3104(d)). In a related provision, the FBSEA mandated that a comprehensive study be prepared and transmitted to Congress, within one year from enactment, on whether foreign banks should be required more generally to conduct all banking operations in the United States through bank subsidiaries rather than through direct branch offices. See FBSEA § 215 and the studies prepared in response to this requirement: *Insured U.S. Branches of Foreign Banks* (revised January 15, 1992), compiled by the FDIC; *Subsidiary Requirement Study*, app. C (Implications for the Deposit Insurance System (Factor 2)) (study prepared by the Secretary of the Treasury and the Board of Governors of the Federal Reserve System (FRB), in consultation with the Comptroller, the FDIC, and the Attorney General of the United States) (submitted on December 18, 1992, by the Secretary of the Treasury to the Chairmen of the Banking Committees of the respective Houses of Congress).

²¹See FBSEA § 214(a), 105 Stat. 2236, 2303. Pursuant to this authority, 52 branches of 27 foreign banks were grandfathered as FDIC-insured institutions on December 19, 1991. The number of insured branches as of October 2002 was approximately 18. The number of insured branches as of July 2011 was approximately 10. The reduction in number has resulted from mergers among foreign banks in their home country, conversion of foreign branches into insured U.S. subsidiary banks, consolidation of branches belonging to a single foreign bank, and outright closure of branches. The statute leaves unclear whether these grandfathered branches could be sold to other foreign banks while retaining their grandfathered status.

otherwise qualified, leading to uncertainty regarding whether nongrandfathered U.S. branches would be prohibited from maintaining any deposit accounts having balances of under the SMDIA, whether or not the account was wholesale in nature. The U.S. bank regulatory agencies issued interim regulations to address this uncertainty,²² and Congress finally resolved the issue in October 1992 by amending the prohibition contained in Section 214(a) of the FBSEA to read “accept or maintain *domestic retail* deposit accounts having balances of less than the SMDIA, and *requiring deposit insurance protection.*”²³ Congress thereby clarified that nongrandfathered branches could continue to accept those initial deposits of less than the SMDIA determined by the appropriate regulator not to require deposit insurance protection.²⁴ In addition, so long as the initial deposit requirement has been satisfied, the amended statutory language has been interpreted to permit (1) subsequent deposits in the same account to be less than the SMDIA, and (2) the account balance itself to fall below the SMDIA.

Thus, regulations of the FDIC and OCC now define the permitted types of deposit-taking activities of nongrandfathered U.S. branches of foreign banks (i.e., those not “requiring deposit insurance protection”) and no longer merely establish the point at which the IBA’s mandatory requirement of FDIC insurance is triggered.

The prohibition on retail deposit-taking activities in Section 214(a) of FBSEA could reflect Congress’s concurrence with the FDIC’s previous opposition to the availability of deposit insurance to U.S. branches of foreign banks. That opposition was based on the FDIC’s concern that such availability would expose the in-

²²The language appeared to prohibit, contrary to the FDIC’s existing regulations, any deposit account balance (including even those of clearing accounts and foreign-source deposit accounts) at a nongrandfathered branch from falling below the statutory threshold of the SMDIA at any time. To avoid significant disruptions in the business of virtually all uninsured branches, the FRB and the Comptroller jointly, on December 19, 1991 (the effective date of the new provision), advised foreign banks that they could continue to rely on existing FDIC regulations defining permissible deposit-taking activities for their uninsured U.S. branches, pending the adoption of further clarifying or interpretive rules. See Statement of December 19, 1991, by the Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency, attached to SR 91-31 (FRB’s Division of Banking Supervision and Regulation) (December 19, 1991, Joint Statement) (concurred in by the FDIC on January 2, 1992).

²³The italicized language was added by amendment on October 28, 1992 as part of the Defense Production Act Amendments of 1992, §§ 302(a), 305(2), Pub. L. No. 102-558, 106 Stat. 4224, 4226 (1992) (codified at 12 U.S.C.A. § 3104(c)).

²⁴See §§ 8:2, 8:3.

insurance fund to unacceptable risks of loss from events beyond the FDIC's control because of limited ability to supervise direct offices of foreign banks.²⁵ As no insured branch of a foreign bank has apparently ever been liquidated by the FDIC, however, this concern would not appear to justify the withdrawal of the option of FDIC insurance for foreign bank branches.

More likely, Section 214(a) of the FBSEA reflected Congress's view that the availability to foreign banks of an elective option for one or more of their branches to become FDIC-insured was inconsistent with the treatment afforded to domestic banks, which enjoyed no such option. This inconsistency was resolved when Congress chose to prohibit foreign bank branches from engaging in those retail deposit-taking activities that required such insurance. In light of the fact that the vast majority of foreign bank branches had already elected not to be FDIC-insured, this prohibition seems to have been preferable from the perspective of foreign banks to requiring all U.S. branches of foreign banks to become FDIC-insured.

Even after the passage of FBSEA's prohibition on deposit-taking activities requiring insurance, there was continued concern in Congress about the overall competitive balance between domestic and foreign banks. This concern was addressed in Section 107 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal Act). That section—while permitting foreign banks to establish direct branch offices interstate on essentially the same basis as domestic banks—contained a set of other provisions entitled “Equalizing Competitive Opportunities for United States And Foreign Banks.” In particular, the Riegle-Neal Act established new, more rigorous restrictions on the authority of uninsured branches of foreign banks to accept initial deposits in amounts less than the SMDIA.²⁶

In directing the bank regulatory agencies to amend their

²⁵See § 8:2. Little if any legislative history exists discussing congressional intent in enacting § 214(a) of the FBSEA.

²⁶The Riegle-Neal Act § 107, Pub. L. No. 103-328, 108 Stat. 2338, 2358 to 64 (1994) (“Equalizing Competitive Opportunities for United States and Foreign Banks”). Another equalizing provision was the imposition of all federal and state consumer protection-oriented laws to all U.S. branches and agencies, and U.S. commercial lending company subsidiaries, of foreign banks to the extent they engage in the relevant regulated activities. Section 107 also contained a new prohibition on managing, through a non-U.S. office of a foreign bank managed or controlled by a U.S. branch or agency (i.e., an offshore shell branch), “any type of activity” impermissible for a non-U.S. office or subsidiary of a U.S. bank under the FRB's Regulation K. In addition, Section 109 subjected any U.S. branch of a foreign bank established outside the foreign bank's home state after

regulations to ensure that foreign banking organizations did not have an unfair competitive advantage over U.S. banking organizations, Congress also directed them, through Section 107(b)(2) of the Riegle-Neal Act, to “consider whether to permit” uninsured branches to accept initial deposits of less than the SMDIA from six classes of depositors:

1. Individuals who are not citizens or residents of the United States at the time of the initial deposit;
2. Individuals who are not citizens of the United States, but are resident in the United States and employed by a foreign bank, foreign business, foreign government, or recognized international organization;
3. Persons to whom the branch or foreign bank has extended credit or provided other nondeposit banking services;
4. Foreign businesses and large U.S. businesses;
5. Foreign governmental units and recognized international organizations; and
6. Persons who are depositing funds in connection with the issuance of a financial instrument by the branch for the transmission of funds.

Moreover, Section 107(b)(3) of the Riegle-Neal Act provided that any de minimis exception must not exceed 1% of the average deposits at the branch. The implementation by the FDIC (with respect to state branches) and OCC (with respect to federal branches) of these provisions is discussed in Section 8:3[2].

While the issue of whether U.S. branch offices of foreign banks should be given access to, or even required to obtain, FDIC insurance has been characterized by some level of inconsistency in the past, the legal framework has now stabilized with the passage of the FBSEA and Riegle-Neal Act. However, significant policy issues relating to foreign bank branches remain. These issues include: (1) treatment of foreign banks’ U.S. operations in comparison with domestic commercial banks;²⁷ (2) the ability of U.S. cities to maintain or enhance their status as international

September 29, 1994, to CRA-like “deposit production office” prohibitions, which became effective June 1, 1997. More recently, as another example of an equalizing measure, the OCC clarified that a federal branch or agency may establish or maintain an operating subsidiary in the same manner as a national bank. Operating Subsidiaries of Federal Branches and Agencies, 65 Fed. Reg. 49,093 (Sept. 26, 2001) (codified at 12 C.F.R. Pts. 5 and 28).

²⁷U.S. branches of foreign banks constitute at present the only significant category of commercial banks operating in the United States that are not subject to a mandatory requirement of federal deposit insurance. This relatively unique status naturally attracts political concerns from time to time over the possibility

financial centers by attracting direct branch offices of foreign banks;²⁸ (3) the FDIC's reluctance to insure deposits at branch offices of foreign banks over which it exercises no overall supervision;²⁹ and (4) the relatively unique "wholesale" and limited purpose nature of most foreign bank branches.³⁰ Given the stability of the current system, even after the financial crisis in 2008 and in light of the passage of the Dodd-Frank Act, however, additional legislative developments in this area will most likely await another crisis specifically involving foreign banks.³¹

§ 8:3 FDIC regulations affecting uninsured branches of foreign banks

The regulations governing insurance of deposits for federal and state branches are substantially similar. These regulations are summarized in Sections 8:3 and 8:4, with the differences between requirements for federal and state branches noted.

of unfair competitive advantage. *See, e.g.*, Federal Reserve Board Staff Analysis of Arguments Relating to Competitive Advantages of Foreign Banks, Appendix A to Letter from Alan Greenspan, Chairman, Federal Reserve Board, to the Hon. Stephen L. Neal, Chairman, Subcomm. on Financial Institutions Supervision, Regulation and Deposit Insurance of the House Comm. on Banking, Finance and Urban Affairs, 1-3 (May 25, 1994) (FRB Staff Analysis of Competitive Advantages). This would appear to be the case particularly when deposit insurance assessments and other costs associated with attracting retail deposits are relatively high for domestic banks, and deposit insurance may be considered more of a regulatory burden than a privilege facilitating access to lower-cost domestic retail sources of funding. As long as virtually all domestic commercial banks are required to maintain FDIC insurance and pay deposit insurance premiums without regard to whether they are retail or wholesale in their U.S. operations, these political concerns would appear likely to resurface from time to time. *See* § 8:1 for a discussion of insurance requirements applicable to virtually all domestic commercial banks.

²⁸*See, e.g.*, Subsidiary Requirement Study, note 15, app. C, 1, 6; *see also* 140 Cong. Rec. S12, 781 to 784 (daily ed., Sept. 13, 1994) (floor remarks of Senator Graham (D-Fla.) during debate on H.R. 3841, the Riegle-Neal Act, preceding Senate passage of the conference report).

²⁹*See* discussion earlier in this section.

³⁰*See* discussion earlier in this section.

³¹The financial services reform legislation that was passed in late 1999, the Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338 (1999), included a number of provisions reportedly designed to address the competitive balance between domestic and foreign banks. *See, e.g.*, § 103(a) (directing the Federal Reserve, in the context of foreign bank elections to be treated as "financial holding companies," to apply "comparable capital and management standards" as apply to domestic banks). That reform legislation, however, did not change the basic deposit insurance requirements for foreign bank operations in the United States.

[1] General Rule

An uninsured foreign bank branch, whether state or federal, may not engage in domestic deposit-taking activities requiring deposit insurance protection.³² The FDIC's regulations define "domestic retail deposits" as the acceptance of "any initial deposit of less than the SMDIA."³³ The term "initial deposit" is defined as "the first deposit transaction between a depositor and the branch where there is no existing deposit relationship."³⁴ The OCC definitions are almost exactly the same.³⁵ State and federal uninsured branches are not deemed to be engaged in domestic retail deposit taking if their initial deposits of less than the SMDIA are derived solely from certain sources or otherwise in the aggregate do not exceed a de minimis amount.³⁶

[2] Exemptions and the De Minimis Rule**[a] Source of Deposit Exemptions**

Responding to the competitive concerns expressed in the Riegle-Neal Act, the FDIC's notice of proposed rulemaking concluded that, "as a group, uninsured U.S. branches of foreign banks do not compete with United States banking organizations for retail deposits."³⁷ The FDIC also stressed that, in determining the types of depositors from which uninsured branches could accept deposits of less than the SMDIA, the groups identified in Section 107(b) of the Riegle-Neal Act were merely to be considered by the FDIC and were not binding on the agency.³⁸

Thus, while the FDIC's amendments provided that uninsured state-licensed branches would be permitted to accept initial

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³²See 12 U.S.C.A. § 3104(c).

³³12 C.F.R. § 347.202(e).

³⁴12 C.F.R. § 347.202(m). The initial deposit may be placed in different kinds of deposit accounts and may be aggregated for purposes of meeting the SMDIA threshold, if held by the same depositor in the same capacity and with the same rights. The FDIC's regulations give no guidance on what period of time would be covered by "existing." In addition, the term "deposit" is broadly defined and means the same as "in Section 3(l) of the Federal Deposit Insurance Act (12 U.S.C. § 1813(l))." 12 C.F.R. § 347.202(c).

³⁵See 12 C.F.R. § 28.11(p).

³⁶See 12 C.F.R. §§ 28.16(b), 347.215.

³⁷60 Fed. Reg. 36,074, 36,075 (1995). Indeed, citing research conducted by the Comptroller, the FDIC concluded that "United States banking organizations are competing quite well with their foreign counterparts operating in the United States."

³⁸See 60 Fed. Reg. 36,074, 36,075 (1995).

deposits of less than the SMDIA from the six categories of depositors specified in Section 107(b)(2)(A) through (F) of the Riegle-Neal Act,³⁹ the FDIC refined and expanded the list of exceptions identified by Congress.

First, the FDIC modified the so-called “nondeposit banking services exception” of the Riegle-Neal Act. The Act called on the FDIC to “consider” permitting uninsured branches to accept initial deposits of less than the SMDIA from persons to whom the branch or foreign bank has extended credit or provided nondeposit banking services. The FDIC modified this exception by:

- (i) requiring that the extension of credit or provision of other nondeposit banking services occur within the previous 12 months,⁴⁰
- (ii) including persons with whom the branch or foreign bank has entered into a written agreement to extend credit or provide other nondeposit banking services within 12 months following the initial deposit,⁴¹
- (iii) including credit or other nondeposit banking services received from an affiliate of the branch or foreign bank,⁴² and
- (iv) including credit or other nondeposit banking services received (or to be received) by immediate family members of a depositor.⁴³

Second, the FDIC clarified and expanded the exception for foreign or large U.S. businesses. With respect to foreign businesses, the FDIC added an exception for “persons from whom an Edge Corporation may accept deposits under Section 211.4(e)(1) of Regulation K” of the Board of Governors of the Federal Reserve System (FRB).⁴⁴ The term “large United States business” was defined to include any entity organized under the law of the United States or any state, provided (1) the entity’s securities are registered on a national securities exchange or quoted on

³⁹See 12 C.F.R. § 347.215.

⁴⁰See 12 C.F.R. § 347.215(a)(3).

⁴¹See 12 C.F.R. § 347.215(a)(3).

⁴²See 12 C.F.R. § 347.215(a)(3). The FDIC stressed that this modification only applies to foreign bank affiliates that are capable of extending credit or providing some other nondeposit banking service. See 61 Fed. Reg. 5671, 5672 (1996). The FDIC explicitly rejected commenters’ proposals to include services obtained by affiliates of the depositor and to add depository services to the exception.

⁴³See 12 C.F.R. § 347.215(a)(3).

⁴⁴12 C.F.R. § 347.215(a)(4), citing 12 C.F.R. § 211.6(a)(1).

NASDAQ, or (2) the entity has annual gross revenues in excess of \$1 million for the fiscal year immediately preceding the initial deposit.⁴⁵

Third, the FDIC clarified the exception for “persons who are depositing funds in connection with the issuance of a financial instrument by the branch for the transmission of funds” to reach electronic funds transfers.⁴⁶

Fourth, the FDIC retained a previously existing exception for deposits either from the federal government or from state governments.⁴⁷

The FDIC’s amendments granted uninsured state-licensed branches five years to reclassify initial deposits received prior to April 1, 1996, into one of the new exceptions or into the reduced *de minimis* exception.⁴⁸ The requirement to reclassify or divest preexisting deposits applies to all deposit accounts that were originally accepted pursuant to any of the exceptions previously set forth in 12 C.F.R. § 346.6(a). The FDIC noted, however, that preexisting deposits that were not subject to the initial deposit exceptions (because the initial deposit establishing the account was equal to or greater than the SMDIA) would not have to be reclassified or divested even if the first new deposit after April 1, 1996, was less than the SMDIA.⁴⁹

The Comptroller published its proposed amendments implementing Section 107(b) of the Riegle-Neal Act on July 5, 1995, as part of a comprehensive revision of regulations governing the international operations of national banks and the operation of foreign banks in the United States through federal branches and agencies.⁵⁰ The Comptroller’s revisions were published in final

⁴⁵See 12 C.F.R. § 347.202(p).

⁴⁶12 C.F.R. § 347.215(a)(6).

⁴⁷See 12 C.F.R. §§ 347.215(a)(5) and 347.215(b). The FDIC also revised the procedures by which an uninsured state-licensed branch can apply for an exemption to accept deposits of less than the SMDIA from other depositors. See 12 C.F.R. § 347.206(b). Such applications must now demonstrate that permitting the deposits will not give the foreign bank an unfair competitive advantage over domestic banks.

⁴⁸See 12 C.F.R. § 347.215(c).

⁴⁹See 61 Fed. Reg. 5671, 5673 (1996). In the case of time deposits, the transition deadline is the first maturity date after April 1, 1996; see also 62 Fed. Reg. 37,748, 37,771 (1997).

⁵⁰See 60 Fed. Reg. 34,907 (1995).

form on May 2, 1996.⁵¹

Like the FDIC's revised rules, the Comptroller's notice of proposed rulemaking observed that, "as a group, uninsured United States offices of foreign banks do not compete [with United States banking organizations] for retail deposits."⁵² The Comptroller also noted, like the FDIC, that it was not limited by the classes of depositors identified in Section 107(b) of the Riegle-Neal Act when identifying the parties from whom uninsured federal branches would be permitted to accept initial deposits of less than the SMDIA.⁵³

Again, like the FDIC's revisions, the Comptroller's final amendments authorized uninsured federal branches to accept initial deposits of less than the SMDIA from the six categories of depositors specified in Sections 107(b)(2)(A) through (F) of the Riegle-Neal Act (and listed in Section 8:3[2][a]).⁵⁴ In addition, the Comptroller modified these statutory exceptions in the same manner and to the same extent as did the FDIC.⁵⁵ The five-year transition period for uninsured federal branches to reclassify preexisting initial deposits also parallels the transition period adopted in the FDIC regulations.⁵⁶

[b] The De Minimis Rule

In addition to exempting certain types of deposits from the SMDIA initial deposit requirement, both the FDIC and OCC rules provide a de minimis exception that permits an uninsured branch to accept a limited amount of initial domestic retail deposits of less than the SMDIA.⁵⁷ The de minimis rule currently permits the acceptance of such deposits if two requirements are satisfied. First, the amount of deposits under the SMDIA (for which no other exemption is available) must not exceed, on an average daily basis, 1% of the branch's deposits for the last 30 days of the most recent calendar quarter.⁵⁸ Second, the branch must not solicit deposits from the general public such as by advertising or

⁵¹See 61 Fed. Reg. 19,524 (1996).

⁵²60 Fed. Reg. 34,907, 34,912 (1995).

⁵³See 60 Fed. Reg. 34,907, 34,912 (1995).

⁵⁴See 12 C.F.R. § 28.16(b).

⁵⁵See 12 C.F.R. § 28.16(b); 61 Fed. Reg. 19,524, 19,536 (1996).

⁵⁶See 12 C.F.R. § 28.16(f).

⁵⁷12 C.F.R. §§ 28.16(b)(9), 347.215(a)(7).

⁵⁸See 12 C.F.R. §§ 28.16(b)(9), 347.215(a)(7). Excluded from the average amount of deposits are deposits of other offices, branches, or agencies or wholly owned subsidiaries of the bank. The FDIC regulation provides that the average

displaying signs.⁵⁹

In its final rule, the FDIC specifically noted that its redrafting of the de minimis rule was not intended to change the manner in which the de minimis amount is calculated.⁶⁰ According to the FDIC, the de minimis amount is calculated as a fraction, with the numerator consisting of the total amount of deposits accepted under the de minimis exception (*not* just the amount of the initial deposits of less than the SMDIA that were accepted to open the accounts). The denominator of the fraction consists of the average amount of third-party deposits maintained by the branch during the last 30 calendar days of the most recent calendar quarter.⁶¹ Thus, the FDIC's comprehensive revision of the regulations governing the activities of foreign banks in the United States clarified (but did not modify) the calculation methodology for the de minimis rule.

[c] Specific Exemptions by Application

Federal or state branches proposing to accept an initial deposit of less than the SMDIA and not otherwise exempted technically are still able to apply to the Comptroller, in the case of federal branches, or the FDIC in the case of state branches, for permission to accept the deposit.⁶² However, in the wake of the Riegle-Neal Act's requirement that the FDIC consider further restrictions on the types of initial deposits under the SMDIA that can be accepted by U.S. branches of foreign banks, it seems unlikely, absent unusually compelling circumstances, that the FDIC or the OCC would issue an exemptive order allowing otherwise ineligible deposits to be paid into such a branch.

[3] Optional Insurance

On its face, Section 214(a) of the FBSEA does not bar foreign bank branches from obtaining deposit insurance. Rather, it only

daily balance shall be computed by using the sum of the close of business figures for the last 30 calendar days including the last business day of the calendar quarter, and dividing by 30. At one time, the FDIC proposed to delete the de minimis exemption. *See* 53 Fed. Reg. 41,180, 41,181 (1988). The FDIC was persuaded by the comments on the proposed regulations from industry sources to retain the rule to allow leeway for inadvertent or small retail deposits. 54 Fed. Reg. 14,064 (1989).

⁵⁹12 C.F.R. §§ 28.16(b)(9), 347.215(a)(7).

⁶⁰*See* 61 Fed. Reg. 5,671, 5,674 (1996).

⁶¹*See* 61 Fed. Reg. 5,671, 5,674 (1996).

⁶²For federal branches, *see* 12 C.F.R. § 28.16(c); for state branches, *see* 12 C.F.R. § 347.215(b). Neither the OCC nor the FDIC is aware of any applications for exemptions pursuant to these regulations ever being filed.

prohibits such branches from engaging in certain retail deposit-taking activities associated with the need for insurance. Thus, branches of foreign banks theoretically remain eligible to apply for FDIC insurance.

Of course, the prohibition found in FBSEA means that even if a nongrandfathered branch of a foreign bank were to successfully apply for and obtain deposit insurance, it would still be unable to accept or maintain domestic retail deposit accounts having balances of less than the SMDIA, and requiring deposit insurance protection.⁶³ Thus, this prohibition would, obviously, render such deposit insurance essentially pointless from a business perspective.

For this reason, it is questionable whether the FDIC would ever approve an application for deposit insurance submitted by a branch of a foreign bank. In fact, the FDIC has eliminated the provision whereby branches of foreign banks could apply for deposit insurance. The FDIC, in rescinding the provision, stated that its action does not “affect a foreign bank’s ability to argue that it may make an application” for insurance for a federal or state branch.⁶⁴ However, the FDIC also observed that “[a]s a practical matter, however, the FDIC does not foresee many circumstances in which it could be appropriate for the FDIC Board of Directors to approve such an application.”⁶⁵

In 2005, the FDIC rejected a request from the Institute of International Bankers to reconsider this last observation. The FDIC explained that while “there are arguments that can be made for providing deposit insurance coverage to wholesale U.S. branches of foreign banks,” there are also “compelling arguments that can be made against providing such coverage.”⁶⁶

The FRB’s statements on continued eligibility for FDIC insur-

⁶³See 12 U.S.C.A. § 3104(c).

⁶⁴63 Fed. Reg. 17,056, 17,066 (1998).

⁶⁵63 Fed. Reg. 17,056, 17,066 (1998).

⁶⁶70 Fed. Reg. 17,557. The arguments the IIB advanced in favor of insuring wholesale branches included the following:

- The FDIC’s approach ignores significant changes in regulatory practices and structures that have occurred since 1991 with regard to foreign banks; broader acceptance of the principle of “investor choice”; and rejection of a broader policy to force foreign banks to operate in the U.S. only through subsidiaries;
- Wholesale depositors often seek the benefits of FDIC insurance—even though the full amount of their deposits may not be insured. The ability to offer these benefits through a U.S. branch would provide a benefit to customers and increase a foreign bank’s funding options;

ance have been contradictory and, to some extent, result-driven. On December 19, 1991, a joint statement was released by the FRB and the Comptroller (in which the FDIC concurred on January 2, 1992) which, among other things, stated that “in accordance with the terms and intent of Section 214(a) [of FBSEA], foreign banks may not establish new insured branches after [December 19, 1991].”⁶⁷ Subsequently, in the context of considering in 1993 whether uninsured U.S. branches of foreign banks

- Optional FDIC insurance is likely to be attractive primarily to foreign banks already operating FDIC-insured branches and subsidiaries in the U.S. and to a relatively small number of other foreign banks, especially those seeking to serve particular ethnic markets. As a result, a more liberal policy likely would have a minimal effect on the deposit insurance fund; and
- Permitting wholesale branches to obtain deposit insurance is consistent with the business model that has been followed by some major U.S. banks that have retained insurance while focusing on wholesale markets.

70 Fed. Reg. 17,556. The FDIC cited the following counterarguments:

- Difficulty in reconciling the idea that Congress imposed the subsidiary requirement with regard to domestic retail deposit activity requiring deposit insurance for the protection of the FDIC with the implicit assumption that Congress did not believe such protection of the FDIC was needed with regard to wholesale branches of foreign banks because customer deposits up to the SMDIA in a wholesale branch would be insured to the same extent as deposits maintained in any other FDIC insured depository institution;
- Unlike bank subsidiaries, branches function as an integral part of the foreign bank itself and do not have their own independent board of directors. Thus, the directors of a foreign bank are not usually subject to the U.S. jurisdiction, and domestic branch personnel essential to explaining certain transactions could be transferred beyond the reach of U.S. authorities;
- Essential records could also be difficult to reach if they are kept at the head office or at branches in other countries;
- A U.S. branch could be subjected to requirements under foreign laws or to political or economic decisions of a foreign government that conflict with domestic bank regulatory policies;
- Operating through a branch, as opposed to subsidiary structure, allows foreign banks the ability to engage in transactions with the home office without significant operational restrictions that might otherwise be applied to transactions with affiliates of insured U.S. banks; and
- Due to the operating relationship of a branch to its home office and dependence on the home office for financial support, the insolvency of a foreign bank with a multinational branch structure will result in the insolvency of the branches, and this may pose complicated and time-consuming issues regarding the resolution of the branch that could more likely be avoided in situations involving banking subsidiaries.

70 Fed. Reg. 17,556 to 17,557.

⁶⁷December 19, 1991, Joint Statement at 2. This position was reiterated on December 18, 1992, in the Subsidiary Requirement Study, app. C, at 13.

were depository institutions “eligible to apply” for FDIC insurance, and thus subject to the Truth in Savings Act and the FRB’s Regulation DD thereunder, the FRB reportedly reversed itself on this interpretation and concluded that Section 214(a) of the FBSEA did not foreclose the eligibility of such offices for FDIC insurance; rather, it merely foreclosed their engaging in the types of deposit-taking activities that would “require deposit insurance protection.”⁶⁸ In May 1994, however, FRB staff repeated its original statement that “(a) foreign bank may not establish a new insured branch after [December 19, 1991].”⁶⁹

[4] Notification Requirements for Uninsured Branches

Even though uninsured branches, as a practical matter, are excluded from attaining FDIC insurance, they must still comply with certain notification requirements.⁷⁰ Each uninsured branch must display conspicuously a sign at each location where it usually receives deposits stating that the FDIC does not insure its deposits.⁷¹ Additionally, the FDIC requires either each signature card, passbook, and instrument (including negotiable certificates of deposit) evidencing a deposit must include the statement “This deposit is not insured by the FDIC,” or else the branch must require that each depositor sign a statement acknowledging that such deposits are not FDIC insured.⁷² The OCC requires a statement similar to the FDIC’s on each signature card, passbook, and instrument evidencing a deposit.⁷³ These notification provisions are an attempt to address the concern of bank regulators that many depositors in the United States assume all of their deposits are federally insured. The FDIC has recommended, but has not yet required, that uninsured branches consider periodically notifying each depositor of the uninsured status of the branch’s deposits.⁷⁴

⁶⁸Memoranda from Lawrence R. Uhlick, Executive Director and General Counsel of the Institute of International Bankers, to Member Bank Voting Representatives re Truth-in-Savings—Regulation DD (May 5 & May 7, 1993).

⁶⁹FRB Staff Analysis of Competitive Advantages at 2.

⁷⁰See 12 C.F.R. §§ 28.16(e), 347.216.

⁷¹See 12 C.F.R. §§ 28.16(e), 347.216(a).

⁷²12 C.F.R. § 347.216(b).

⁷³See 12 C.F.R. § 28.16(e).

⁷⁴See 54 Fed. Reg. 27,154 (1989). The FDIC suggested in 1989 that an annual notification of the uninsured status would be appropriate.

In 1991, with enactment of the Federal Deposit Insurance Corporation Improvement Act (FDICIA), all U.S. depository institutions not having federal deposit insurance were generally subjected to disclosure requirements of their

§ 8:4 FDIC requirements for insured branches

As noted previously,⁷⁵ approximately 10 insured branches of foreign banks remained in operation as of July 2011. In view of the reduced number of such branches, this section only briefly highlights a number of the unique and stringent compliance obligations of such institutions under regulations of the FDIC.⁷⁶ In particular, each foreign banking organization maintaining an insured branch must agree to: (1) provide certain information; (2) be examined; and (3) comply with additional rules in the areas of record-keeping and reporting, pledging of assets, and asset maintenance.⁷⁷

nonfederally insured status, as promulgated by the Federal Trade Commission (FTC). *See* Pub. L. No. 102-242, § 151, 105 Stat. 2236, 2282 to 2285 (1991) (codified at 12 U.S.C.A. § 1811); 105 Stat. 2236, 2282—85 (1991) (codified at 12 U.S.C.A. § 1831t). Although these disclosure requirements appear applicable to uninsured U.S. branches of foreign banks as well as all other depository institutions in the United States, the deposits of which are not federally insured, Congress has consistently (since enactment of the FDICIA in 1991) expressly denied the FTC any authority to expend funds to implement or enforce § 151 of FDICIA. *See* Pub. L. No. 102-395, 106 Stat. 1828 (1992) (FY 1993 FTC appropriations); Pub. L. No. 103-121, 107 Stat. 1153 (1993) (FY 1994 FTC appropriations); Pub. L. No. 103-317, 108 Stat. 1724 (1994) (FY 1995 FTC appropriations). Thus, only the notice and disclosure requirements of the regulations of the Comptroller and the FDIC are currently enforced against uninsured branches of foreign banks.

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⁷⁵*See* § 8:2.

⁷⁶*See* 12 C.F.R. Pt. 347. As in the case of any FDIC-insured bank, insured branches of foreign banks must pay deposit insurance assessments to the FDIC. *See generally* 12 C.F.R. Pt. 327. However, FDIC-insured status also triggers a number of other generally applicable U.S. bank-regulatory requirements. These include, for instance, the CRA, 12 U.S.C.A. §§ 2901 to 2906; federal law restrictions on loans to insiders, 12 U.S.C.A. § 1828(j)(2); and restrictions on transactions between an insured bank and an affiliated company, 12 U.S.C.A. § 371c, c-1. The Riegle-Neal Act also clarified and affirmed that all U.S. branches and agencies of foreign banks, including insured branches, must comply with both state and federal laws imposing “requirements that protect the rights of consumers in financial transactions, to the extent that the [office] engages in activities that are subject to such laws.” § 107(c)(1), Pub. L. No. 103-328, 108 Stat. 2338, 2360 (1994) (codified at 12 U.S.C.A. § 3106(a)). The regulatory consequences of FDIC insurance are not as significant as they once were for branches of foreign banks, in light of the fact that foreign banks (other than those with grandfathered branches) must now organize or acquire an insured U.S. bank subsidiary in order to engage in retail deposit-taking activities.

⁷⁷*See* 12 C.F.R. §§ 347.204 to 347.205, 347.209 to 347.211. The FDIC’s regulations with respect to examinations, information, record-keeping, and asset pledge and maintenance requirements also apply to “foreign banks” organized under the laws of Puerto Rico, Guam, American Samoa, and the

[1] Affiliate Information and Examinations

In connection with any deposit insurance application for a U.S. branch or subsidiary, a foreign bank must enter into an agreement with the FDIC.⁷⁸ Pursuant to the agreement, the insured branch or subsidiary must provide the FDIC with information in English concerning the affairs of the foreign bank and its affiliates located outside the United States. The purpose of the information is to assist the FDIC in determining the branch or subsidiary's relationship with its affiliates and the effect of such relationship on the branch or subsidiary.⁷⁹ For the same purposes, a foreign bank with an insured branch or subsidiary is obligated to provide information regarding the affairs of, and to permit the FDIC to examine, any office, agency, branch, or affiliate of the foreign bank located in the United States.⁸⁰ In order to enable the FDIC to enforce its supervisory authority, the foreign bank must also consent to personal jurisdiction in the United States and appoint an agent for the service of process.⁸¹

Foreign banks that are not subject to comprehensive consolidated supervision (CCS)⁸² may be subject to additional conditions. Such conditions may include an agreement permitting the FDIC to examine the foreign bank and its offices and affiliates *outside* the United States.⁸³

In certain instances, the laws of a foreign bank's home country could restrict the FDIC's ability to take advantage of the commit-

Virgin Islands to the extent they are "insured banks" solely by virtue of their having an insured branch in one of the 50 states or the District of Columbia. See 12 C.F.R. § 347.202(g). In 1985, the FDIC eliminated the option of posting a surety bond in place of, or in addition to, its pledge of assets based on the possibility that the FDIC would not be able to obtain expeditious payment. See 49 Fed. Reg. 49,614 (1984).

⁷⁸See 12 C.F.R. § 347.204(a).

⁷⁹See 12 C.F.R. § 347.204(a)(1).

⁸⁰See 12 C.F.R. § 347.204(a)(2).

⁸¹See 12 C.F.R. § 347.204(a).

⁸²See §§ 1:1 et seq.

⁸³70 Fed. Reg. 17,553 n.6. The FDIC initially proposed to require all foreign banks to agree to permit FDIC examination of the foreign bank and affiliates located outside the United States. International Banking, 69 Fed. Reg. 43,060, 43,066 (Jul. 19, 2004). The Institute of International Bankers objected, stating that such a requirement would be an inappropriate extraterritorial exercise of supervisory authority and would likely conflict with the laws of most home countries. In the Final Rule, the FDIC agreed not to require such a commitment from foreign banks that were determined by the appropriate federal banking agency to be subject to CCS. However, it reserved the right to demand this and other commitments from banks not subject to CCS. 70 Fed. Reg. 17,553 n.6.

ments made by the foreign bank. FDIC regulations previously provided that, in such circumstances, the foreign bank should enter into the agreement to extent permitted by such laws, but that the FDIC reserved the right to reject the application if the foreign bank was unable to provide the FDIC with sufficient information.⁸⁴ In 2005, the FDIC revised the regulation to state simply that the FDIC “will consider” such restrictions, as well as the willingness of the foreign bank to seek waivers and exemptions from such restrictions, in deciding whether to grant or deny the foreign bank’s deposit insurance application.⁸⁵ “In this situation, it is envisioned that the foreign bank would be responsible for addressing and resolving these issues in consultation with the appropriate FDIC staff.”⁸⁶

[2] Record-Keeping

Each insured branch must keep accounts and records in English of its daily transactions and activities.⁸⁷ Such records must be kept on a separate, branch-by-branch basis.⁸⁸ A foreign bank with more than one insured branch in a particular state may, however, treat such branches as a single entity for purposes of compliance with the FDIC’s record-keeping requirements.⁸⁹

[3] Pledge of Assets

A foreign bank with an insured branch must pledge assets to and for the benefit of the FDIC to be used to protect the deposit insurance fund from losses should the FDIC become obligated to pay off the insured deposits of the branch.⁹⁰ Generally, each insured branch of the foreign bank must meet the asset pledge requirement separately; however, a foreign bank with more than one insured branch in any state may treat all of its insured branches in the state as one entity for purposes of complying

⁸⁴See 12 C.F.R. § 347.208(a)(1)(ii) (2004).

⁸⁵See 12 C.F.R. § 347.204(b).

⁸⁶69 Fed. Reg. 43,066.

⁸⁷See 12 C.F.R. § 347.205.

⁸⁸See 12 C.F.R. § 347.205.

⁸⁹See 12 C.F.R. § 347.205.

⁹⁰See 12 C.F.R. § 347.209(a). The FDIC’s position with respect to the pledge of assets is that “[t]he very essence of the pledge of assets is that the assets pledged should be as free from risk and as liquid as possible in order to provide sure and immediate protection to the [FDIC] if an insured branch should fail.” 49 Fed. Reg. 49,614, 49,615 (1984).

with this requirement.⁹¹

[a] Amount of Assets to Be Pledged

The amount of assets to be pledged to the FDIC is based on a percentage of the insured branch’s liabilities, excluding liabilities to other offices and wholly owned subsidiaries of the foreign bank. Previously, branches were generally required to pledge assets equal to 5% of third-party liabilities. However, in 2005, the FDIC modified the asset pledge requirement to make it more risk-based. Under the new system, newly insured branches are required to pledge 5% of the projected third-party liabilities at the end of each of their first three years of operations.⁹² All other insured branches are placed into supervisory risk groups based on supervisory evaluations provided by the branch’s primary federal regulator. For each group, the FDIC requires the pledge of a specified percentage of average third-party liabilities for the last 30 days of the calendar quarter, depending on the branch’s asset maintenance level, as follows:⁹³

	Asset Maintenance Level		
	<u>Equal to or greater than 108%</u>	<u>Equal to or greater than 106%</u>	<u>Less than 106%</u>
Supervisory risk group A	2	4	6
Supervisory risk group B	3	5	7
Supervisory risk group C	4	6	8

Supervisory risk group A consists of “financially sound institutions with only a few minor weaknesses.”⁹⁴ Supervisory risk group B consists of “institutions that demonstrate weaknesses which, if not corrected, could result in significant deterioration of the institution and increased risk of loss to the deposit insurance fund.”⁹⁵ Supervisory risk group C consists of “institutions that pose a substantial probability of loss to the deposit insurance

⁹¹See 12 C.F.R. § 347.209(b)(5).

⁹²See 12 C.F.R. § 347.209(b)(1).

⁹³See 12 C.F.R. § 347.209(b)(2).

⁹⁴12 C.F.R. § 347.209(b)(3)(i).

⁹⁵12 C.F.R. § 347.209(b)(3)(ii).

fund.”⁹⁶

[b] Types of Assets Permitted to Be Pledged

The FDIC’s regulations list the types of assets that may be pledged, which are limited to U.S. dollar denominated assets. Eligible assets consist of bank certificates of deposit with maturities of less than one year;⁹⁷ interest bearing obligations of, or fully guaranteed by, the United States or any of its agencies or instrumentalities;⁹⁸ highly rated commercial paper;⁹⁹ banker’s acceptances with a maturity not greater than 180 days;¹⁰⁰ highly rated general obligations of, or guaranteed by, any state of the United States, or any county, municipality, or subdivision thereof;¹⁰¹ obligations of certain international development banks;¹⁰² and highly rated notes issued by unaffiliated U.S. bank holding companies, banks, or U.S. branches or agencies of a foreign bank.¹⁰³ The FDIC may determine other assets to be eligible.¹⁰⁴

In 2005, the FDIC expanded the types of certificates of deposit, bankers’ acceptances, and banking institution notes that may be pledged. Whereas previously, branches could only pledge such

⁹⁶12 C.F.R. § 347.209(b)(3)(iii).

⁹⁷See 12 C.F.R. § 347.209(d)(1). Eligible certificates of deposit must be payable in the United States and issued by a banking institution that has executed a valid waiver or offset agreement. Certificates of deposit issued by any foreign bank branch or agency that is not an affiliate of, or from the same country as, the pledging bank are included. Insured deposit notes, payable in the United States and with a remaining maturity of less than one year, are considered certificates of deposit. See FDIC Interpretive Letter, December 14, 1987.

⁹⁸See 12 C.F.R. § 347.209(d)(2). The guarantee must extend to both principal and interest.

⁹⁹See 12 C.F.R. § 347.209(d)(3). The commercial paper must be rated P-1 or P-2 or their equivalent by a nationally recognized rating service. If there is a conflict in ratings, the lower one must be used.

¹⁰⁰See 12 C.F.R. § 347.209(d)(4). A bankers’ acceptance issued by a foreign bank branch or agency that is not an affiliate of or from the same country as the pledging bank is eligible. The bankers’ acceptance must be payable in the United States.

¹⁰¹See 12 C.F.R. § 347.209(d)(5). The obligations must not be in default with respect to either interest or principal; they must have a credit rating within the two rating categories of a nationally recognized rating service.

¹⁰²See 12 C.F.R. § 347.209(d)(6). These banks are The African Development Bank, Asia Development Bank, Inter-American Development Bank, and International Bank for Reconstruction and Development.

¹⁰³See 12 C.F.R. § 347.209(d)(7). The notes must have a rating within the two higher rating categories of a nationally recognized rating service.

¹⁰⁴See 12 C.F.R. § 347.209(d)(8).

instruments if they were issued by banks (or, in the case of notes, bank holding companies), branches are now also permitted to pledge instruments issued by savings associations and savings and loan holding companies. On the other hand, the FDIC added a requirement that pledged certificates of deposit be negotiable, although nonnegotiable CDs pledged prior to March 18, 2005, were grandfathered until maturity.¹⁰⁵

[c] Depository

The foreign bank must deposit the assets required to be pledged in a FDIC-approved depository.¹⁰⁶ The depository may be an unaffiliated insured state bank, national bank, or insured U.S. branch of a foreign bank.¹⁰⁷ The FDIC has the right to dismiss any approved depository that fails to perform fully its obligations under the pledge agreement.¹⁰⁸ The act of placing the assets with the depository constitutes a valid pledge to the FDIC.¹⁰⁹

[d] Pledge Agreement

The foreign bank must enter into a pledge agreement, satisfactory in form and substance to the FDIC, with the depository governing the assets pledge of each insured branch.¹¹⁰ The pledge agreement must provide for the kind and amount of assets to be pledged,¹¹¹ the pledge of additional assets,¹¹² the substitution of assets,¹¹³ the delivery of title transfer documents,¹¹⁴ the responsibilities of the depository,¹¹⁵ reporting requirements,¹¹⁶ access to pledged assets for the FDIC and the pledgor,¹¹⁷ the release by the

¹⁰⁵See 70 Fed. Reg. at 17,555 to 17,556.

¹⁰⁶See 12 C.F.R. § 347.209(c).

¹⁰⁷See 12 C.F.R. § 347.209(c).

¹⁰⁸See 12 C.F.R. § 347.209(c).

¹⁰⁹See 12 C.F.R. § 347.209(d).

¹¹⁰See 12 C.F.R. § 347.209(e).

¹¹¹See 12 C.F.R. § 347.209(e)(1).

¹¹²See 12 C.F.R. § 347.209(e)(2).

¹¹³See 12 C.F.R. § 347.209(e)(3). The FDIC permits the substitution of assets of equivalent or greater value for pledged assets. The FDIC may suspend or terminate this right of substitution.

¹¹⁴See 12 C.F.R. § 347.209(e)(4). The regulations require the foreign bank to provide copies of all such documents to the appropriate regional director concurrently with their delivery.

¹¹⁵See 12 C.F.R. § 347.209(e)(5). The depository must maintain the pledged assets separate from all other assets and unencumbered by any claim the depository might assert against the pledged assets. The pledged assets may be held in book-entry form.

depository of pledged assets to the pledgor or the FDIC,¹¹⁸ the disposition of interest earned on pledged assets,¹¹⁹ the expenses and fees of the depository,¹²⁰ and the resignation or discharge of the depository and appointment of a successor.¹²¹ The FDIC retains the right to waive compliance with the pledge agreement.¹²²

[4] Asset Maintenance

The FDIC requires that an insured branch of a foreign bank maintain, on a daily basis, eligible U.S. dollar assets (or assets denominated in a currency freely convertible into U.S. dollars) in an amount not less than 106% of the preceding quarter's average book value of the branch's liabilities excluding those due to other offices or wholly owned subsidiaries of the foreign bank.¹²³ "Eligible assets" exclude the following assets: assets due from any of the foreign bank's other offices or affiliates, certain assets classified as impaired, any deposit of the branch of a bank that has not executed a valid waiver of offset agreement, any asset not supported by sufficient credit information, any asset not in the bank's possession or to which it cannot show good title, and any intangible asset.¹²⁴ If the foreign bank has more than one insured branch in the same state, the foreign bank may treat all those branches as a single entity for purposes of compliance with

¹¹⁶See 12 C.F.R. § 347.209(e)(6). The depository and the pledging foreign bank must provide to the appropriate regional director of the FDIC detailed initial and quarterly reports on the assets pledged. The FDIC may require additional reports from time to time.

¹¹⁷See 12 C.F.R. § 347.209(e)(7).

¹¹⁸See 12 C.F.R. § 347.209(e)(8), (9).

¹¹⁹See 12 C.F.R. § 347.209(e)(10). The foreign bank is entitled to any interest earned on the pledged assets unless the FDIC directs some other disposition.

¹²⁰See 12 C.F.R. § 347.209(e)(11). The FDIC will not be responsible for the expenses or fees of a depository.

¹²¹See 12 C.F.R. § 347.209(e)(12).

¹²²See 12 C.F.R. § 347.209(e)(13).

¹²³See 12 C.F.R. § 347.210(a). See also 12 C.F.R. § 347.210(d) for guidance in computing average book value of branch liabilities. This asset maintenance requirement replaces the capital equivalency requirement that existed prior to the July 1989 amendments to Part 346 of the FDIC's regulations. See 54 Fed. Reg. 14,064 (1989). For a newly established branch, the amount is based on the estimated book value at the end of the first full quarter of operation. See 12 C.F.R. § 347.210(a) (clause two of first sentence). See § 8:3 for a discussion of the theoretical availability of deposit insurance for nongrandfathered branches.

¹²⁴See 12 C.F.R. § 347.210(b). The regulations allow the FDIC to exclude any other asset it does not consider bankable. See 12 C.F.R. § 347.210(b)(7).

the asset maintenance requirements.¹²⁵

¹²⁵*See* 12 C.F.R. § 347.210(c).