Chapter 1

Forms of Entry, Operation, Expansion, and Supervision of Foreign Banks in the United States

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§ 1:1 Introduction

Over the past 35 years, foreign banks have grown from a small presence in the United States into a major component of the U.S. commercial banking market. Despite somewhat adverse changes in the U.S. regulatory climate for foreign banks—including a sustained increase in the degree of federal supervision to which they are subject—foreign banks have significantly increased their share of the U.S. banking market during this period.[1] The 1999 passage of the Gramm-Leach-Bliley Act (GLB Act)[2] removed a number of federal restrictions on nonbanking activities for both foreign and domestic banking organizations.

The legal framework applicable to foreign banks operating in the United States is in many ways the framework applicable to domestic banks.[3] This reflects the guiding principle of "national treatment," or parity of treatment between domestic and foreign banks, that has informed U.S. legislation affecting foreign banks since the International Banking Act of 1978 (IBA).[4] Although the IBA has been amended numerous times, it continues to provide the general legal framework under which foreign banks operate in the United States.[5]

Foreign banks conduct their U.S. operations through a variety

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[Section 1:1]

[1]The share of total assets of U.S. offices of foreign banks rose from 3.8% in 1973 to 22.0% in 2011. Foreign banks achieved similar market-share increases in total loans, business loans, and total deposits. *See* Federal Reserve Board, Share Data for U.S. Offices of Foreign Banking Organizations (as of September 2011), available at www.federalreserve.org (FRB Share Data). *FRB Share Data* is a report prepared by the Board and updated quarterly. It provides dollar volume and market-share information of the assets, loans, and deposits of all foreign bank offices in the United States and, separately, of those in New York and California. Unless otherwise indicated, citations are to the *Share Data Report* updated in September 2011. Likewise, unless otherwise indicated, citations to the Federal Reserve's quarterly *Structure Data Report* on the number and type of foreign bank operations in the U.S. (*see* discussion later in this section) are to the most recent version, which was published September 2011.

[2]The Gramm-Leach-Bliley Act of 1999, Pub. L. No. 106-102, 113 Stat. 1338 (GLB Act).

[3]As used in the IBA and this chapter, the term "foreign bank" means "any company organized under the laws of a foreign country . . . which engages in the business of banking." 12 U.S.C.A. § 3101(7).

[4]The International Banking Act of 1978, Pub. L. No. 95-369, 92 Stat. 607 (codified at 12 U.S.C.A. §§ 3101 to 3108 and in scattered sections of 12 U.S.C.A.).

[5]The IBA has been amended by: Act of Sept. 14, 1979, Pub. L. No. 96-64, 93 Stat. 412; the Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, §§ 704 to 705, 96 Stat. 1469, 1539 to 1540; the Competitive Equality Banking Act of 1987, Pub. L. No. 100-86, § 204, 101 Stat. 552, 584 (CEBA), the Foreign Bank Supervision Enhancement Act of 1991, tit. II, subtit. A of the Federal Deposit Insurance Corporation Improvement Act of 1991, Pub. L. No. 102-242, §§ 201 to 215, 105 Stat. 2286 223 to 305 (FBSEA), the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, Pub. L. No. 103-328, 108 Stat. 2338 (Riegle-Neal Act); and the Economic Growth and Regulatory Paperwork Reduction Act of 1996, div. A, tit. II of the Omnibus Consolidated Appropriations Act, 1997, Pub. L. No. 104-208, 110 Stat. 3009-499 (EGRPRA).

of forms, including federal or state-licensed branches (the predominant form), agencies, commercial bank subsidiaries, commercial lending companies, and representative offices. The choice of form affects the foreign bank's regulatory treatment, its permissible scope of activities, its opportunities for geographic expansion within the U.S., and determines the identity of its regulators. Thus, the selection of an appropriate vehicle for U.S. banking is a crucial strategic decision for a foreign bank. The principal forms in which foreign banks conduct their U.S. operations are described in Section 1:3 (Forms of Entry and Operation) and are listed in Appendix 1A.

At the time of the IBA's passage in 1978, there were 268 U.S. operations of foreign banks[6] with assets of $109.1 billion.[7] As of September 30, 2011, 316 operations of foreign banks controlled approximately $3.35 trillion in assets.[8] The table below shows the growth of foreign banks' U.S. operations since 1978 based on information from the Board of Governors of the Federal Reserve System (the Board). As the table demonstrates, while the number of U.S. operations has declined in recent years, the volume of assets, deposits, and loans controlled by U.S. offices of foreign banks has risen steadily since 1978.

Selected Assets and Liabilities of U.S. Offices of Foreign Banks[9]

(Figures are in billions of dollars, except Number of Operations)

Year *(Year-End, Unless Noted)*	**Number of Operations***	**Total Assets****	**Business Loans**	**Total Loans**
1978	268	$109.1	$32.7	$65.3
1983	557	328.8	84.5	192.4
1988	675	650.6	167.3	338.8
1993	704	855.7	195.6	379.6

The IBA was further amended by the Financial Services Regulatory Relief Act of 2006, Pub. L. No. 109-351, 120 Stat. 1966 § 709 and the Dodd-Frank Act.

6. *See* International Banking Act of 1978: Hearings Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing, and Urban Affairs, 95th Cong., 2d Sess. 46 (Table 22) (1978) (IBA Senate Hearings).

7. Federal Reserve Board, Share Data for U.S. Offices of Foreign Banks (as of September 2002), available at http://www.federalreserve.gov.

8. Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

9. Federal Reserve Board, Share Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.org.

Year (Year-End, Unless Noted)	Number of Operations*	Total Assets**	Business Loans	Total Loans
1998	538	1,117.9	280.2	494.2
June 2002	396	1,373.2	252.8	492.3
June 2006	320	2,193.9	294.1	807.0
March 2008	318	2,754.3	391.6	985.7
December 2010	313	2,944.2	326.6	960.5
September 2011	316	3,398.7	363.9	1,598.7

* The Board's data cover foreign bank branches and agencies in 50 states and the District of Columbia, New York investment companies (through 1996), U.S. commercial banks that are more than 25% owned by foreign banks, and International Banking Facilities. Representative offices and Edge Act corporations are excluded.

** Adjusted to exclude net claims on own foreign offices.

As a percentage of the entire U.S. banking market, the U.S. operations of foreign banks grew steadily from 1978 until the early 1990s, at which point they stabilized and then declined modestly. The table below shows the share of the entire U.S. banking market (including domestic and foreign-owned banking operations) attributable to U.S. operations of foreign banks.[10]

Ratio of Foreign Banks' U.S. Operations to all Banks in the United States[11]

(Figures are in percentages)

Year (Year-End, Unless Noted)	Total Assets*	Business Loans	Total Loans
1978	8.0%	13.1%	8.8%
1983	14.6	18.3	15.6
1988	19.6	28.2	16.9
1993	21.2	33.8	17.0
1998	19.1	28.5	14.6
June 2002	19.6	25.6	12.4
June 2006	22.4	26.0	14.4
March 2008	23.7	27.2	15.0
December 2010	20.5	25.1	13.7

[10]Data for offshore shell branches managed or controlled by U.S. offices of foreign banks are included beginning in 1993.

[11]Federal Reserve Board, Share Data for U.S. Offices of Foreign Banks (as of September 2011), available at http://www.federalreserve.org.

Year *(Year-End, Unless Noted)*	Total Assets*	Business Loans	Total Loans
September 2011	22.0	25.7	14.9

* Adjusted to exclude net claims on own foreign offices.

As the table shows, foreign banks account for a significant share of the U.S. banking market, particularly with respect to commercial lending. Foreign banks historically have participated more in wholesale banking than retail banking in the U.S.[12] Overall, however, foreign banks have become fully assimilated in virtually every area of U.S. banking. By all accounts, foreign banks have contributed to meeting the credit needs of the U.S. economy, financing foreign investment, maintaining the pace of financial innovation, and globalizing the U.S. banking markets.[13]

The modest decline in foreign banks' U.S. operations in recent years can be attributed to a number of factors. The increasingly competitive nature of the U.S. financial markets and the globalization of financial services have required foreign and domestic banks alike to reevaluate their U.S. business strategies. Some foreign banks have chosen to focus their U.S. efforts more narrowly on wholesale banking or other commercial services that do not require the opening of extensive branch networks. During the same time frame, foreign banks have experienced increased regulatory scrutiny from the Board and other U.S. banking agencies, particularly after the enactment of the Foreign Bank Supervision Enhancement Act of 1991 (FBSEA).[14]

Even so, foreign and domestic banking organizations have been granted enhanced freedom to engage—in the U.S. market—in a wide range of business activities, including nonbanking activities such as securities underwriting and dealing, merchant banking, and insurance underwriting and dealing.[15] This expanded authority results from the GLB Act's modernization of the U.S. banking system, which had frequently been criticized for enforcing outdated "line-of-business" restrictions on banking organizations (e.g., prohibiting certain kinds of securities and insurance

[12] *See* § 1:2.

[13] *See, e.g.*, Institute of International Bankers, ECONOMIC BENEFITS TO THE UNITED STATES FROM THE ACTIVITIES OF INTERNATIONAL BANKS: FINANCIAL SERVICES IN A GLOBAL ECONOMY (1998); Foreign Banks—Assessing Their Role in the U.S. Banking System, (GAO/GGD-96-26) (Feb. 1996).

[14] Pub. L. No. 102-242, 105 Stat. 2286. *See* discussion earlier in this section.

[15] *See generally* § § 9:1 et seq. and 10:1 et seq.

activities). Among other things, the GLB Act allows foreign and domestic banks to engage in financial activities, as well as certain nonfinancial activities, through "financial holding companies" and "financial subsidiaries."[16] In similar fashion, the Riegle-Neal Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)[17] lifted most barriers to geographic expansion of banking activities in the U.S. for both foreign and domestic banks. Consequently, foreign banks operating in the United States face greater regulatory scrutiny but also enjoy greater business opportunities than ever before.

The terrorist attacks of September 11, 2001, resulted in additional scrutiny of international banking transactions in the United States, whether conducted by domestic or foreign banks. The International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (IMLA) requires foreign banks and other financial institutions to implement extensive new policies and procedures to combat international money laundering.[18] IMLA and its implementing regulations have added another layer of regulatory scrutiny to the U.S. operations of foreign banks.

Most recently, the Dodd-Frank Act, enacted in July 2010 as a response to the financial crisis in the fall of 2008, effected sweeping changes to the U.S. financial regulatory landscape, including in merging the Office of Thrift Supervision into the Office of the Comptroller of the Currency, establishing a council of regulators, known as the Financial Stability Oversight Council ("FSOC"), to monitor threats to U.S. financial stability, and establishing the Consumer Financial Protection Bureau to enforce consumer financial laws. Although the Dodd-Frank Act did not substantially alter the regulatory framework for foreign banks, the Act will change the manner and potentially the extent to which foreign banks operate in the United States. In particular, Dodd-Frank enables the FSOC to designate systemically important foreign nonbank financial companies for enhanced prudential supervision by the Federal Reserve. The Act's "Volcker Rule" prohibits, with several important exceptions, foreign banks' proprietary trading and relationships with private equity and hedge funds unless such activities meet a rigorous test for occurring "solely outside the United States." Dodd-Frank also imposes new capital

[16]*See* § 1:2.

[17]*See* Dodd-Frank Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[18]Pub. L. No. 107-56, § 326, 115 Stat. 272, 296. IMLA was part of the USA PATRIOT Act, which was signed into law on October 26, 2001. *See* Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act), Pub. L. No. 107-56.

and liquidity requirements with respect to foreign banks operating in the United States and limits foreign banks' conduct of certain swap activities. Many of these provisions remain the subject of extensive agency rulemaking processes that will determine the specific impact to foreign banks' operation in the United States.

This chapter is intended to provide a road map of the regulatory structure governing the commercial banking operations of foreign banks in the United States and to introduce the specialized topics treated in the chapters that follow. Section 1:2 outlines the statutory and regulatory framework for the regulation of foreign bank operations in the U.S. Section 1:3 examines the various vehicles available for foreign banks to enter and participate in the U.S. banking market. Section 1:4 examines supervisory and enforcement issues that are increasingly important to foreign banks, particularly on international money laundering concerns. Section 1:5 provides a brief conclusion.

§ 1:2 Statutory and regulatory framework

[1] Background

This section summarizes the principal federal statutes and regulations governing the U.S. operations of foreign banks. The trend over time generally has been toward parity in treatment of foreign and U.S. banks; more extensive federal oversight of foreign banks, including through a stricter, more penalty-based enforcement system; and greater operating flexibility for U.S. and domestic banks alike.

Prior to the IBA, foreign banks that conducted business in the U.S. generally did so (and continue to do so) through U.S. branches, agencies, and representative offices rather than through subsidiary banks chartered in the United States. By structuring their operations this way, the U.S. operations of foreign banks were licensed and regulated primarily by state banking authorities.[19] Structuring their operations this way also avoided the restrictions on interstate banking and branching and on engaging in certain kinds of financial activities that applied to U.S. banks and bank holding companies.

[Section 1:2]

[19] *See, e.g.*, Conference of State Bank Supervisors v. Conover, 715 F.2d 604, 606 (D.C. Cir. 1983) ("Prior to the adoption of the [International Banking Act], a bank organized under the laws of a foreign country could obtain a charter from a state authority only; the federal government did not charter foreign banks.") (quoting H.R. Rep. No. 95-910, 2d Sess. 5 (1978)).

The IBA changed that landscape dramatically. Its guiding principle of "national treatment" resulted in restrictions on the activities and interstate operations of foreign banks that were comparable, but not identical, to the restrictions applicable to U.S. banking organizations. Federal regulation increased, and in 1991, Congress vested the Federal Reserve Board with primary and extensive authority over all U.S. operations of foreign banks (though in certain instances, the Office of the Comptroller of the Currency (OCC) or other regulators serve as the primary supervisory authority in coordination with the Board). In the succeeding 10 years, Congress substantially eliminated the financial activity and geographic restrictions applicable to both U.S. and foreign banks alike (but with some important exceptions and unique consequences for foreign banks). Legislative responses to the September 11, 2001, terrorist attacks have subjected foreign banking organizations (FBO) to greater scrutiny for policing international money laundering activity. In addition, most recently, the Dodd-Frank Act effected substantial change to the regulatory framework for U.S. banking entities and foreign banking entities alike, including in the areas of systemic risk regulation, proprietary trading and private equity and hedge fund investments, and investor protection. In sum, foreign banks operating in the United States have substantial operating flexibility to engage in virtually any financial activity in virtually any location, but they are subject to more extensive federal regulation than ever before.

[2] The International Banking Act of 1978

The IBA was enacted after several years of growing concern in Congress regarding the perceived inadequacy of federal supervision of foreign bank operations in the United States, as well as concern that the relative lack of oversight gave foreign banks an unfair competitive advantage. While recognizing that foreign banks had generally behaved in a responsible manner, Congress was prompted by the sheer "number and size of foreign banking operations, and their ever-increasing importance to the structure of the banking system" to enact a comprehensive federal regulatory structure to govern their operations.[20]

The guiding principle of the IBA is "national treatment," mean-

[20] S. Rep. No. 95-1073, 2d Sess. 2 (1978), reprinted in 1978 U.S.C.C.A.N. 1421 (IBA Senate Report). By 1978, 122 foreign banks were operating in the U.S. with combined assets of $90 billion. As of April 1978, foreign bank offices had more than $26 billion in outstanding commercial and industrial loans, which was approximately 20% of the similar outstanding loans by large U.S. banks at the time.

ing "parity of treatment between foreign and domestic banks in like circumstances."[21] The IBA therefore reduced or eliminated many of the competitive advantages that foreign banks enjoyed vis-à-vis domestic banks but at the same time made available to foreign banks opportunities that had previously been confined to U.S. banking organizations.[22]

In terms of new opportunities, Section 2 of the IBA authorized the Comptroller of the Currency to waive the requirement that all directors of national banks be U.S. citizens, a change that made owning a national bank a much more practical option for foreign banks than had previously been the case.[23] Section 3 enabled foreign banks to establish Edge Act corporations, just as domestic banks could, and Section 4 enabled branches and agencies of foreign banks to obtain federal licenses from the OCC, with attendant OCC regulation, instead of being limited to state licenses and state regulation.[24] U.S. branches of foreign banks were also put on the same footing as domestic banks with respect to deposit insurance for retail deposits as they were both authorized and required to obtain such insurance for most retail deposit taking.[25]

In terms of new restrictions, Section 5(a) of the IBA authorized foreign banks to engage in interstate operations only to the extent that such activities were permissible for domestic banks and

[21] *See* S. Rep. No. 95-1073, 2d Sess. 2 (1978), reprinted in 1978 U.S.C.C.A.N. 1421.

[22] *See* Misuraca, Comment: Foreign Banking in the United States: An Objective Study of the International Banking Act of 1978, 4 J. Int'l L. & Prac. 539, 542 (1995). Congress also expected that national treatment would decrease the likelihood of discriminatory treatment of U.S. banks by foreign countries.

[23] 12 U.S.C.A. § 72. The revised provision allows a minority of the directors to be non-U.S. citizens.

[24] 12 U.S.C.A. §§ 611 to 632 (Edge Act corporations, through which U.S. banks may engage in a range of activities outside the country); 12 U.S.C.A. § 3102 (federal branches and agencies, which have comparable powers and regulation as national banks).

[25] 12 U.S.C.A. § 3104. The IBA was later modified by the FBSEA to prohibit branches of foreign banks from either obtaining federal deposit insurance or accepting retail deposit accounts with balances below the SMDIA except through a subsidiary bank that is both chartered in the U.S. and FDIC-insured. 12 U.S.C.A. § 3104(d)(1). Foreign bank branches that had already obtained federal deposit insurance were exempted through a grandfather clause. 12 U.S.C.A. § 3104(d)(2).

bank holding companies;[26] in practice, this required each foreign bank to choose a "home state" for its U.S. operations and confine its activities in other states to those permitted for U.S. banks located in the home state.[27] Likewise, Section 8 limited the ability of foreign banks to engage in nonbanking activities by imposing on their U.S. operations most of the activities restrictions of the Bank Holding Company Act of 1956 (BHC Act).[28] The IBA also required foreign banks to maintain reserves against their liabilities, eliminating a considerable advantage that they had enjoyed over domestic banks.[29]

The IBA clearly achieved Congress's intention of establishing a "federal presence" in the regulation and supervision of foreign bank activities in the United States.[30] In addition, whether operating through a U.S. bank subsidiary or through branches and agency offices, a foreign bank became fully subject for the first time to the dual banking system of overlapping federal and state regulatory regimes; that is, it could freely choose to operate through a national or state bank subsidiary located in its "home state," or it could choose to have its branches or agency offices licensed by either the home state or the OCC.

[3] The Foreign Bank Supervision Enhancement Act of 1991

In the late 1980s and early 1990s, several events prompted Congress to reconsider the adequacy of federal supervision of

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[26] 12 U.S.C.A. § 3103(a)(1) and (2). Multistate branches in existence at the time were grandfathered. 12 U.S.C.A. § 3103(b).

[27] When enacted, the IBA and its regulations required every foreign bank that operated an unrestricted branch or bank subsidiary to designate an IBA "home state" and prohibited it from having an unrestricted branch outside that state, with the exception of grandfathered branches. *See* 12 U.S.C.A. § 3103; 12 C.F.R. § 211.22. The IBA also prohibited a foreign bank from acquiring a bank subsidiary outside of its home state without express statutory permission of the state of the acquisition target. *See* 12 U.S.C.A. § 3102(a). In this way, the IBA effectively made applicable to foreign banks the interstate banking restrictions of the McFadden Act and the BHC Act, which had previously applied only to domestic banks and their holding companies.

[28] 12 U.S.C.A. § 3106 (applying the limitations on nonbanking activities of the BHC Act, 12 U.S.C.A. §§ 1841 et seq., to the U.S. operations of foreign banks). Just as the IBA grandfathered nonconforming branches that existed at the time of enactment, it also grandfathered certain U.S. financial activities in which foreign banks actually engaged in 1978 that were not permissible activities for U.S. bank holding companies. *See* 12 U.S.C.A. §§ 3103(b), 3106(c).

[29] 12 U.S.C.A. § 3105.

[30] S. Rep. No. 95-1073, 2d Sess. 2 (1978), reprinted in 1978 U.S.C.C.A.N. 1421.

foreign banks. In particular, the unforeseen collapse of the Bank of Commerce Credit International (BCCI), despite its extensive U.S. operations, raised serious concerns about the effectiveness of U.S. supervision of foreign banking operations within its borders. These concerns increased with widespread media accounts of unauthorized lending to Iraq by the U.S. operations of Banca Nazionale del Lavoro. Additionally, these events concerning foreign banks occurred against a domestic backdrop of the savings and loan bailout and record commercial bank failures.[31] As Congress responded domestically by increasing the regulation of the thrift and banking industries in 1989[32] and 1991,[33] there was also a perception that action was needed with respect to the U.S. operations of foreign banks. The resulting FBSEA imposed new approval and monitoring requirements on the U.S. operations of foreign banks and substantially increased the overall supervisory role of the Federal Reserve Board.[34]

[a] Prior Board Approval for Establishment of Branches and Other Offices in U.S.

Before 1991, no company, including a foreign bank, could acquire control of a U.S. bank without undergoing a rigorous application and approval process by the Federal Reserve under Section 3 of the BHC Act.[35] However, the Board had no such prior approval power with respect to a foreign bank's establishment of a domestic branch, agency, or representative office in the U.S.

[31]The BCCI was a complex web of shell corporations, affiliates, and subsidiaries that successfully infiltrated the U.S. banking system in the 1980s. Before its exposure and shutdown, BCCI engaged in money-laundering, bribery, and support of criminal activities around the world. *See* Sen. John Kerry & Sen. Hank Brown, *The BCCI Affair: A Report to the Committee on Foreign Relations*, Senate Print No. 102-140, 102d Cong., 2d Sess. (1992), available at http://www.fas.org/irp/congress/1992_rpt/bcci. As noted, the FBSEA was also motivated in part by the billions of dollars in illegal loans by the Banca Nazionale del Lavoro (BNL) to Iraq. *See* Gail et al., The Foreign Bank Supervision Act of 1991: Expanding the Umbrella of "Supervisory Reregulation," 26 Int'l Law. 993, 993 & n.2 (1992).

[32]*See* Federal Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 100 Stat. 183 (FIRREA).

[33]*See* Federal Deposit Insurance Corporation Improvement Act of 1991, Pub. L. No. 102-242, 105 Stat. 2236 (FDICIA).

[34]*See* Letter from Alan Greenspan, Chmn., to the Hon. Donald W. Riegle, Jr. (May 9, 1991) (accompanying Board's proposed FBSEA and analysis of the proposed statutory language), reprinted in 137 Cong. Rec. S5623 to S5629 (daily ed. May 9, 1991); *see generally* Gruson, Foreign Banks Are No Longer Welcome in the United States, 10 Banking Pol'y Rep. 5 (1991) (discussing prevailing regulatory climate at time of FBSEA's enactment).

[35]12 U.S.C.A. § 1842(a).

Instead, the foreign bank needed only to obtain the approval of the state[36] or federal licensing authority for the branch, agency, or office (which was usually the state authority, since relatively few foreign banks had exercised the IBA option of federal licensing from the OCC).

This perceived "gap" led to Section 202 of FBSEA, which requires advance Federal Reserve approval (in addition to the requisite state or OCC license and approval) for a foreign bank to establish any branch, agency, or representative office in the United States.[37] Prior Federal Reserve approval is also required for a foreign bank to upgrade an existing office such as to upgrade an agency to a branch or a representative office to an agency.[38]

Moreover, Congress prescribed specific standards that the Federal Reserve must use in making such determinations; i.e., it may not approve an application for a branch or agency unless it determines that the foreign bank:[39]

1. Engages directly in the business of banking outside of the United States;
2. Is subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in its home country; and[40]

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[36]*See* §§ 4:1 et seq.

[37]12 U.S.C.A. § 3105(d)(1) (branches and agencies); § 3107(a)(1) (representative offices). Such approval was also required for a foreign bank to acquire or take control of a "commercial lending company," which is an organization other than a bank that maintains credit balances permissible for an agency and engages in the business of making commercial loans. *See* 12 C.F.R. § 211.21(g). The FBSEA did not increase the extensive preexisting authority of the Federal Reserve under Section 3 of the BHC Act over the ability of a foreign bank to acquire control of a domestic bank.

[38]12 U.S.C.A. § 3105(d)(1). Prior approval is not required for downgrading an office though the Board must be notified of such a change within 10 days. 12 C.F.R. § 211.24(a)(4). Foreign bank branches, agencies, and representative offices are discussed in § 1:3.

[39]For the establishment of a representative office, these standards are discretionary, not mandatory. *See* 12 C.F.R. § 211.24(d)(2); *see also* 79 Fed. Res. Bull. 805 (Aug. 1993) (*Citizens National Bank*).

[40]EGRPRA modified this requirement to permit the Board to approve an application upon a finding that the foreign bank's home-country authorities "are actively working to establish arrangements for the consolidated supervision of such bank" and all other factors are consistent with approval. 12 U.S.C.A. § 3105(d)(6)(A). In deciding whether to apply this exception, the Board must consider whether (1) the foreign bank "has adopted and implements procedures to combat money laundering," and (2) its home country "is developing a legal regime to address money laundering or is participating in multilateral efforts to

3. Has furnished the information that the Federal Reserve needs to adequately assess the application.[41]

In its discretion, the Federal Reserve also may consider certain other factors in making its determination, i.e., (1) whether the home country has consented to the establishment of the proposed branch or agency; (2) the financial and managerial resources of the applicant bank; (3) whether the bank has provided "adequate assurances" that it will supply the Board with the information necessary for it to exercise its supervisory responsibilities; and (4) whether the foreign bank and its U.S. affiliates are in compliance with applicable U.S. law.[42] The Board also may consider the needs of the community, the bank's operating history, and its relative size in its home country.[43]

[b] Other FBSEA Requirements

The FBSEA also imposed new requirements relating to (1) state-licensed branches or agencies of foreign banks; (2) examination procedures; and (3) deposit insurance. First, Section 202(a), as implemented by the Board, prohibits a state-licensed branch or agency of a foreign bank from engaging in any activity as principal that would be impermissible for a federally licensed

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combat money laundering." 12 U.S.C.A. § 3105(d)(6)(B). In November 2007, the Federal Reserve Board evaluated these two factors with respect to the People's Republic of China and ultimately concluded that China's regulatory structure satisfied the "actively working" standard because of the country's participation in international anti-money laundering fora and newly created anti-money laundering agencies. *See, e.g.*, Fed. Res. Bull. C24 (Mar. 2008) (China Merchants Bank Co., Ltd.); Federal Reserve Order Approving Bank of Communications' Application to Establish a Branch at 3 (Apr. 8, 2011) (updating the various initiatives pursued by the China Banking Regulatory Commission, the primary bank supervisor in China, and the People's Bank of China, the primary anti-money laundering supervisory in China). Finding that a country's bank supervisor exercises supervision in a manner that satisfies this standard has sometimes been difficult. In certain instances, the Board has found that home-country supervision does not meet the statutory standard for establishing a branch or agency but is sufficient to permit establishment of a representative office, in light of the office's limited activities. *See, e.g.*, 82 Fed. Res. Bull. 591 (1996) (Cedel Bank, S.A.); 82 Fed. Res. Bull. 593 (1996) (Commercial Bank "Ion Tiriac," S.A.); 82 Fed. Res. Bull. 599 (1996) (Promstroybank of Russia). In late 2001, the Board adopted a regulation limiting representative office activities in such cases. 66 Fed. Reg. 54345 (Oct. 26, 2001). The factors considered in meeting the standard are discussed in the Board's initial interim regulation. *See* 57 Fed. Reg. 12,992 (April 15, 1992). For additional discussion of the CCS standard, *see* § 1:3.

[41] 12 U.S.C.A. § 3105(d)(2).

[42] 12 U.S.C.A. § 3105(d)(3).

[43] 12 U.S.C.A. § 3105(d)(4).

branch, unless the Board has determined that the activity is "consistent with sound banking practice," and in the case of an insured branch, the FDIC has determined that the activity "would pose no significant risk to the deposit insurance fund."[44] State branches and agencies are subject to the same limitations with respect to loans to a single borrower as are applicable to federally licensed branches and agencies under the IBA.[45]

Second, the FBSEA centralizes examination authority over foreign bank operations squarely in the Federal Reserve Board.[46] The Board is specifically authorized to examine any foreign bank office (including bank subsidiaries) though it is directed to coordinate its examinations with the OCC, FDIC, and state banking authorities where possible.[47] To ensure that foreign bank operations in the U.S. are not subject to duplicative examinations, federal and state regulators have entered into various coordination agreements.[48] The Federal Reserve works with the other federal banking agencies or applicable state authorities as appropriate to coordinate examinations.

Third, Congress affirmed the IBA principle that retail depositors should always have federal deposit insurance for U.S. deposits below the standard maximum deposit insurance amount (SMDIA) in U.S. operations of foreign banks but decided to confine such insurance to state or nationally chartered banks that are subsidiaries of foreign banks. As a result, Section 214(a) of FBSEA generally prohibits branches of foreign banks from accepting or maintaining domestic retail deposit accounts below the SMDIA ($250,000 as of 2011),[49] and the deposits held by such

[44] 12 U.S.C.A. § 3105(h)(1)(A) and (B); 12 C.F.R. §§ 211.21, 211.29 (Board); 12 C.F.R. Pt. 362 (FDIC).

[45] 12 U.S.C.A. § 3105(h)(2). That is, FBSEA requires nationwide "aggregation" of lending activities by all of a foreign bank's branches and agencies. Although FBSEA refers only to aggregation of lending by federally licensed branches and agencies, Regulation K clarifies that the required aggregation includes lending by state-licensed operations as well. *See* 12 C.F.R. § 211.28(a).

[46] 12 U.S.C.A. § 3105(c)(1)(A). Previously, while the Board did have examination authority under the IBA, its powers "were viewed largely as ancillary or residual to those of the OCC, the FDIC, or the appropriate state banking authorities." Gail et al., The Foreign Bank Supervision Act of 1991: Expanding the Umbrella of "Supervisory Reregulation," 26 Int'l Law. 993, 1000 (1992).

[47] 12 U.S.C.A. § 3105(c)(1).

[48] *See* § 1:4.

[49] 12 U.S.C.A. § 3104(d)(1).

branches may not be federally insured.[50] Thus, a foreign bank wishing to offer federal insurance for retail deposits in the U.S. may do so only through a separately chartered U.S. bank or savings association subsidiary.

[4] The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994

The Riegle-Neal Act substantially relaxed federal restrictions on the interstate banking and branching activity of both U.S. and foreign banks. Enacted in response to criticism from both domestic and foreign banks regarding the U.S.'s uniquely restrictive rules on interstate expansion,[51] the Act eliminated most obstacles to providing full banking services in more than one state. The restrictions applicable to foreign banks' interstate branching activities that remained after Riegle-Neal were effectively lifted by the Dodd-Frank Act. The Riegle-Neal Act also placed additional restrictions on foreign banks' offshore shell branch activities and retail deposit taking.

[a] Interstate Expansion

As the result of the Riegle-Neal and Dodd-Frank Acts, there are generally three ways in which a foreign bank may expand its operations geographically beyond the borders of its "home state": (1) acquisition of a bank subsidiary in another state; (2) merger of a bank subsidiary located in another state with a bank subsidiary in its home state; and (3) acquisition of branches and de novo branching in another state. State laws cannot prohibit a foreign bank from engaging in these types of expansion.

[i] Acquisition of Bank Subsidiaries

The Riegle-Neal Act repealed the provision in the BHC Act that had effectively prohibited bank holding companies from owning bank subsidiaries in more than one state. As a result, a bank holding company (BHC) that owns a bank in one state is authorized to acquire a bank in any other state regardless of any state

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[50] The few foreign bank branches that already had obtained FDIC deposit insurance when FBSEA was enacted were permitted to maintain it. 12 U.S.C.A. § 3104(d)(2). There are currently only 10 such branches. FDIC Institution Directory (as of May 12, 2011).

[51] *See generally* Stock and Plotkin, The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, 9 J. Int'l Banking L. 402 (1994). *See also* Mulloy and Lasker, The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994: Responding to Global Competition, 21 J. Legis. 255, 259–269 (1995) (detailing legislative history of Riegle-Neal Act).

law restrictions that might otherwise apply.[52] Acting as a BHC, a foreign bank therefore may acquire a U.S. bank subsidiary in any state even if the foreign bank already owns a bank subsidiary in a different state.[53] The Riegle-Neal Act imposed certain "concentration limits," however, that are intended to ensure that interstate acquisitions of banks do not result in an undue concentration of deposits with one banking organization.[54]

[ii] Mergers of Bank Subsidiaries

The Riegle-Neal Act authorizes an insured bank subsidiary of a BHC, including a foreign bank, to merge with an insured bank with a different home state regardless of state law.[55] The resulting single bank is permitted to maintain the existing branches of each of the previous organizations, and in that way, the bank may operate interstate branches. The resulting bank may also establish or acquire additional branches within each state to the same extent as either bank in the merger could have done so in the absence of the merger.[56]

Although the Act's interstate merger provisions refer to "insured" banks, uninsured branches and agencies of foreign banks may participate in such transactions as well. The IBA specifies that, for purposes of interstate branching and agency operations, a federal branch or agency of a foreign bank is treated as if it were a national bank, and a state branch or agency is treated as if it were a state bank licensed by the IBA home state

[52] 12 U.S.C.A. § 1842(d)(1)(A).

[53] *See* §§ 6:1 et seq.

[54] 12 U.S.C.A. § 1842(d)(2) (e.g., paragraph (A) prohibits a banking organization from controlling more than 10% of deposits nationwide).

[55] 12 U.S.C.A. § 1831u(a)(1). Foreign banks continue to designate an IBA home state despite the liberalized interstate banking rules of the Riegle-Neal and Dodd-Frank Acts. *See* 12 C.F.R. § 211.22. If the foreign bank does not select a home state, the Board is authorized to select one for the bank. 12 U.S.C.A. § 3103(c). For a state-chartered insured bank, the "home state" is the state in which it is chartered; for a national bank, it is the state in which its main office is located. 12 U.S.C.A. § 1831u(4)(g). The FDIC has interpreted the Riegle-Neal Act's merger provisions to allow a foreign bank to transfer its insured branches to an out-of-state bank. *See* Letter of William F. Kroener III, General Counsel of the FDIC to Lawrence R. Uhlick, Executive Director and General Counsel of the Institute of International Bankers (May 13, 1996).

[56] *See* 12 U.S.C.A. § 1831u(d)(2) (states retain the right to determine the authority of a bank to establish more than one branch within its borders). Most States allow full statewide branching for banks otherwise located in the state.

of the foreign bank.[57]

[iii] Branch Acquisitions and De Novo Branching

As is true of U.S. banks generally, the U.S. operations of a foreign bank—whether a branch, agency, commercial lending company, or subsidiary U.S. bank—may directly acquire a branch of another bank located outside the home state of the foreign bank's U.S. operations. Another option for interstate expansion is to establish branches de novo. Prior to the Dodd-Frank Act, the U.S. or foreign bank could only do so if the "host" state had enacted a law that applied equally to all banks and expressly permitted all out-of-state banks to establish de novo branches in that state.[58]

The Dodd-Frank Act relaxed the restrictions on de novo interstate branching as applied to national banks and state-insured banks (and therefore foreign banks).[59] Section 613 of the Dodd-Frank Act permits national banks and state-insured banks to establish a branch in any state if the law of the state in which the branch will be located would permit establishment of the branch by a state bank chartered in the state. Since the IBA bases foreign banks' interstate branching authority on national banks and state-insured banks' authority,[60] Section 613 of the Dodd-Frank Act similarly relaxes the restrictions on de novo interstate branching for foreign banks.

Complications may arise in the event an acquired branch is subject to the Community Reinvestment Act[61] at the time of acquisition. Under ordinary circumstances, only federally insured banks are subject to CRA[62] while uninsured branches of foreign banks are not. However, if a foreign bank acquires a branch in a state in which the foreign bank does not already have a branch, and the acquired branch is subject to CRA, then that branch must remain subject to CRA after the acquisition—even if the foreign bank relinquishes federal deposit insurance for the

[57] 12 U.S.C.A. § 3103(a)(1) (federal branch or agency); 12 U.S.C.A. § 3103(a)(2) (state branch or agency).

[58] 12 U.S.C.A. § § 36(g)(1), 1828(d)(4)(A).

[59] Dodd-Frank Act, Pub. L. No. 111-203, § 613 (2010).

[60] 12 U.S.C.A. § 3103(a).

[61] Title VIII of the Housing and Community Development Act of 1977, Pub. L. No. 95-128, 91 Stat. 1111, 1147 to 1148 (codified as amended at 12 U.S.C.A. §§ 2901 et seq.).

[62] *See* 12 U.S.C.A. § 2902(2).

acquired branch by converting it to an "unrestricted branch."[63]

[b] Prohibition of Deposit Production Offices

Neither a foreign nor U.S. bank may operate an interstate branch as a "deposit production office," i.e., an office that generates deposits without engaging in significant lending in the surrounding community.[64] Specifically, if an interstate branch's loan-to-deposit ratio is less than 50% of the aggregate loan-to-deposit ratios of all banks in the host state, then the appropriate federal banking agency must determine whether the branch is reasonably helping to meet the credit needs of its community.[65] If the agency concludes that it is not, it may order the branch closed, and the bank may be prohibited from establishing other branches in the state.[66]

[c] Retail Deposit Limitations

As described previously, the FBSEA generally prohibited U.S. branches of foreign banks from either offering federal insurance for deposits or accepting initial deposits of less than $100,000 from retail depositors.[67] Such branches were still permitted to accept initial uninsured deposits of less than $100,000 from some types of depositors, however, and the Riegle-Neal Act required the OCC and FDIC to reexamine and write rules regarding the types of depositors that ought to be allowed to make such uninsured deposits. The ensuing regulations limited such depositors to: (1) non-U.S. citizens or residents; (2) resident non-U.S. citizens who are employed by a foreign bank, business, or government or recognized international organization; (3) persons to whom the foreign bank of any affiliate has extended credit or provided nonbanking services in the prior year or with whom the bank or affiliate has a contract to provide such services within the next

[63] *See* 12 C.F.R. § 345.11(c). This requirement does not apply if the foreign bank converts the acquired branch to a "limited branch." Limited branches are discussed in § 1:3[2][d].

[64] 12 C.F.R. §§ 25.63 to 25.64 (OCC), 208.7(c) to (d) (Board), 369.3 to 369.4 (FDIC).

[65] 12 C.F.R. §§ 25.63 to 25.65, 208.7(c) to (e), 369.3 to 369.5. For a U.S. bank, the primary consideration in making this determination is its CRA performance. However, uninsured branches of foreign banks, which generally are not subject to CRA, are not required to develop a record of performance under the CRA in order to satisfy the standard of the deposit production provision. *See* 62 Fed. Reg. 47,732 (1997).

[66] 12 C.F.R. §§ 25.65, 208.7(e), 369.5.

[67] This limit is now the "standard maximum deposit insurance amount" set by the FDIC. As of July 2010, it is $250,000 for most types of accounts. *See* Dodd-Frank Act, Pub. L. No. 111-203, § 335(a)(1) (2010).

year; (4) foreign businesses and "large" U.S. businesses;[68] (5) foreign governmental bodies; (6) U.S. governmental bodies; (7) persons depositing funds in connection with the issuance of a financial instrument by the branch or the transmission of funds by any electronic means; and (8) persons that may deposit funds with an Edge Act Corporation.[69] In addition, the regulations reduced the acceptable level of "de minimis" deposits of under $100,000 from depositors not included in this group from 5% to 1% of the branch's average deposits for the last 30 days of the most recent calendar quarter.[70]

[5] The Gramm-Leach-Bliley Act

Just as the Riegle-Neal Act and Dodd-Frank Act substantially eliminated the restrictions on interstate banking and branching for both U.S. and foreign banks, the GLB Act substantially eliminated the long-standing restrictions on banking organizations engaging in the United States in such plainly financial activities as securities and insurance underwriting. Enacted in 1999, the GLB Act authorizes both U.S. and FBOs to engage in virtually any *financial* activity in the United States.[71]

The GLB Act did not change the basic structure of U.S. regulation of foreign banks. However, certain requirements must be satisfied in order to engage in financial activities in accordance with the Act, and some of these requirements have unique consequences for foreign banks. Sections 9:1 et seq. and 10:1 et seq. describe in detail the permissible nonbanking activities for U.S. operations of foreign banks and include a thorough discussion of the sweeping changes made by the GLB Act. Section 1:2[5] merely provides highlights of several key provisions affecting foreign banks.

[a] Financial Holding Company Requirements

The GLB Act provides two vehicles that a banking organization can use to engage in financial activities or affiliate with

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[68] A "large" U.S. business is one that is either registered on a stock exchange, quoted on the National Association of Securities Dealers Quotation System (NASDAQ), or has annual gross revenue of more than $1 million. 12 C.F.R. §§ 28.11(r), 347.202(p).

[69] 12 C.F.R. §§ 28.16(b) (OCC), 347.215(a) (FDIC).

[70] 12 C.F.R. §§ 28.16(b)(9)(i), 347.215(a)(7).

[71] As discussed in greater detail in § 10:8, the Dodd-Frank Act prohibits banking organizations from engaging in certain types of proprietary trading and from sponsoring and investing in private equity or hedge funds.

financial companies.[72] The first and most flexible vehicle is a "financial holding company," which allows financial activities to be conducted through nonbanking subsidiaries of a BHC. The second is a "financial subsidiary," which allows financial activities to be conducted through direct subsidiaries of a bank. As between the two, the financial holding company has been the preferred vehicle for both domestic and foreign banking organizations in part because it can engage in certain financial activities, such as merchant banking and insurance underwriting, that a financial subsidiary cannot.[73] As of this writing, 48 foreign companies had become financial holding companies.[74]

A financial holding company (FHC) is a BHC that satisfies certain regulatory requirements. That is, to be a financial holding company, a BHC's subsidiary depository institutions must all be "well capitalized," "well managed," and rated "satisfactory" or better in their most recent CRA examinations. All three requirements have objective criteria that are prescribed in detail in federal banking regulations.[75] A BHC that meets these three requirements can engage through nonbanking subsidiaries in financial activities. It may also engage in these and any other permitted financial activities merely by filing an after-the-fact notice with the Federal Reserve rather than undergoing the cumbersome application-and-prior-approval process that can apply to bank holding companies more generally.[76]

Consistent with the national treatment principle, a FBO that satisfies the three requirements may use the financial holding company vehicle to engage in the same broad range of financial activities as a U.S. BHC that satisfies these requirements. That process is straightforward where the foreign bank conducts its operations in the United States exclusively through federally insured U.S. banking subsidiaries. In that case, the foreign bank is plainly a BHC, and each of its U.S. bank subsidiaries must

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[72] *See* §§ 10:1 et seq.

[73] Financial subsidiaries are described in greater detail in §§ 10:1 et seq.

[74] Federal Reserve Board, Financial Holding Companies (as of April 28, 2011), available at http://www.federalreserve.gov/generalinfo/fhc/.

[75] 12 U.S.C.A. § 1843(l); *see* 12 U.S.C.A. § 1841(o)(9) and 12 C.F.R. 225.2(s)(1) (definition of "well managed"); 12 C.F.R. § 225.2(r)(2)(i) (definition of "well capitalized"); 12 U.S.C.A. § 2906(b)(2) and 12 C.F.R. § 25.28 (criteria used in assigning CRA ratings).

[76] 12 U.S.C.A. § 1843(k)(6). *See* §§ 10:1 et seq. However, the Dodd-Frank Act requires financial holding companies to obtain Federal Reserve approval before acquiring a company with total consolidated assets of more than $10 billion. *See* Dodd-Frank, § 604(e)(2.

satisfy the three requirements in exactly the same manner as the subsidiary banks of a domestic BHC.

The situation is more complicated where a foreign bank conducts its operations in the U.S. directly through branches and agencies. The issue is the application of the "well capitalized" and "well managed" requirements where the foreign bank's U.S. operations are not distinct from the foreign bank itself but rather are an integral part of the bank as is the case with branches and agencies. In these circumstances, the GLB Act required the bank regulators to apply "comparable capital and management standards" as apply to domestic banks.[77]

In 2001, the Federal Reserve Board issued final regulations to carry out this congressional directive. First, the Board determined that the "well capitalized" requirement must be applied not merely to the U.S. operations of the foreign bank but instead to the entire organization. The rules establish two methods for a foreign bank to satisfy that requirement.

The first applies to a foreign bank whose home-country supervisor has adopted capital standards consistent with the Capital Accord of the Basel Committee on Banking Supervision (the Basel Accord). A foreign bank qualifies under this standard if its total and Tier 1 risk-based capital ratios, as calculated under its home-country standard, are at least six percent for Tier 1 capital to total risk-based assets and 10% for total capital to risk-based assets.[78]

The second method applies to either a foreign bank whose home-country supervisor has not adopted the Basel Accord standards or to a foreign bank that does not satisfy the standards of the first method. In these circumstances, a foreign bank may nevertheless qualify as "well capitalized" if it obtains from the Board an advance determination that its capital is "otherwise comparable" to that required of a well-capitalized U.S. bank.[79]

In contrast to the "well capitalized" requirement, the Federal Reserve's rules provide that the "well managed" requirement may be satisfied solely by reference to a foreign bank's U.S.

[77] 12 U.S.C.A. § 1843(l)(3).

[78] 12 C.F.R. § 225.90(b)(1). The Board will also consider a foreign bank's leverage ratio for purposes of "comparability review" under 12 C.F.R. § 225.92(e), but a specific leverage ratio standard was deleted from the final regulations. *See* Federal Reserve Board, Bank Holding Companies and Change in Bank Control, 66 Fed. Reg. 400, 408 (Jan. 3, 2001) (final rule implementing financial holding company provisions of the GLBA). *See also* §§ 2:1 et seq.

[79] 12 C.F.R. § 225.90(b)(2).

branches, agencies, and commercial lending companies (as opposed to the entire foreign bank): each must have achieved at least a "satisfactory" rating on a composite basis during its most recent examination by federal regulators.[80] Additionally, the foreign bank's home-country supervisor must consent to the expansion of the bank's activities, and its management must meet standards comparable to that required of a U.S. bank owned by a financial holding company.[81]

[b] Nonconforming Activities

Prior to enactment of the GLB Act, so-called "Qualifying Foreign Banking Organizations" (QFBOs) were permitted by Federal Reserve regulation to engage outside the United States, and indirectly inside the United States, in certain activities that were not permitted for domestic bank holding companies, including nonfinancial activities. Permitting broader activities for QFBOs was intended to ensure that U.S. nonbanking restrictions would not have an undue extraterritorial effect on foreign banks that were authorized by their home country to affiliate with companies engaged in activities that were not permissible for U.S. bank holding companies—even where the QFBO engaged in such "nonconforming" activities in the United States.[82] While the GLB Act permitted greater combinations of banking and *financial* activities, it reinforced the separation between banking and *nonfinancial* activities. Nevertheless, the IBA allows a QFBO—even one that elects to be treated as an FHC—to continue to engage in nonfinancial activities to the same extent as before the Act's enactment.[83]

Under the IBA, some foreign banks also had "grandfathered" authority to engage in both financial and nonfinancial activities that were prohibited for domestic bank holding companies. Although its relevance has waned with the passage of time, the GLB Act provides that if such a foreign bank elects to be treated as an FHC, it forfeits its right to engage in grandfathered *finan-*

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[80] 12 C.F.R. § 225.90(c)(1).

[81] 12 C.F.R. § 225.90(c)(2) and (3).

[82] A foreign bank qualifies as a QFBO if "more than half of its worldwide business is banking; and more than half of its banking business is outside the United States." 12 C.F.R. § 211.23(a).

[83] *See* §§ 10:1 et seq.

cial activities that are otherwise permissible for an FHC.[84] However, such a foreign bank may continue to engage in any *nonfinancial* activities grandfathered by the IBA.[85]

[c] Prudential Safeguards

The GLB Act expressly authorizes the Board to impose restrictions on the relationships or transactions between a U.S. branch, agency, or commercial lending company of a foreign bank and any U.S. affiliate.[86] Before enactment of the GLB Act, the Board had imposed such safeguards—most notably the limitations of Sections 23A and 23B of the Federal Reserve Act (FRA)—on transactions between a U.S. branch or agency of a foreign bank and its U.S. affiliates engaged in certain securities underwriting and dealing activities.[87] In November of 2002, the Board exercised its GLB Act authority by extending the limitations of Sections 23A and 23B of the FRA to transactions between a U.S. branch, agency, or commercial lending company of a foreign bank and any U.S. affiliate engaged in financial activities under the GLB Act, including securities underwriting and dealing, merchant banking, and insurance underwriting.[88]

[6] The USA PATRIOT Act of 2001

On October 26, 2001, President Bush signed into law the USA PATRIOT Act, a legislative response to the terrorist attacks of September 11.[89] A key part of that legislation is the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (IMLA), which amended the Bank Secrecy Act (BSA),[90] the primary U.S. anti-money laundering (AML) statute. Prior to the enactment of IMLA, the BSA and related regulations already imposed a number of record-keeping and reporting obligations on foreign banks' agencies, branches, and subsidiaries and included the requirements to file suspicious activity reports (SAR) and

[84] Additionally, even if such a bank does not become an FHC, the Board now has discretion to restrict its participation in grandfathered financial activity that is permissible for an FHC.

[85] 12 U.S.C.A. § 3106(c)(3)(A).

[86] 12 U.S.C.A. § 3106(c)(3)(B). *See* §§ 5:1 et seq.

[87] *See* 62 Fed. Reg. 45,295, at 45,304 (Aug. 27, 1997) (adopting final Operating Standards applying Sections 23A and 23B of FRA to transactions between U.S. branches and agencies of foreign banks and their "Section 20" securities affiliates).

[88] 12 C.F.R. § 223.61.

[89] Pub. L. No. 107-56, 115 Stat. 272.

[90] Pub. L. No. 91-508, tit. I & II, 84 Stat. 1114 (codified as amended at 12 U.S.C.A. §§ 1951 et seq. and 31 U.S.C.A. §§ 5311 et seq.).

currency transaction reports (CTR).[91] IMLA added several new provisions to the BSA. In addition, the terrorist attacks and the subsequent enactment of IMLA reinvigorated AML enforcement by U.S. banking regulators.

The additional requirements of IMLA, coupled with the new enforcement climate, have substantially increased the compliance burden across the U.S. banking sector, including for foreign banks and their U.S. branches, agencies, and subsidiaries. Banking institutions in the U.S. have devoted significant resources in the past ten years to compliance with the new AML regulations and beefed-up examination standards. In addition, a wave of AML-related enforcement actions have hit U.S. banking institutions and foreign banks, a phenomenon that looks to continue well into the future.[92]

[a] Required Anti-Money Laundering Programs

Section 352(a) of IMLA requires every "financial institution" to establish an antimoney-laundering program.[93] An anti-money laundering program consists of internal policies, procedures, controls, and staff training to prevent and detect the use of the financial institution's accounts for money-laundering.

"Financial institution" is broadly defined in IMLA by reference to the BSA, and expressly includes insured banks, agencies, or branches of foreign banks in the U.S., commercial lending banks or trust companies, private bankers, credit unions, thrifts, registered broker-dealers, futures commission merchants, and money service businesses.[94] This significantly expands the previous federal requirement to maintain such a program, which covered only federally insured depository institutions.[95] Thus, while uninsured branches and agencies of foreign banks were already subject to a number of the BSA's requirements (such as the obligation to report certain currency transactions or suspicious activity),[96] they were generally not required to implement anti-money laundering programs until IMLA.

The final Treasury rule, effective October 28, 2002, specifies that a financial institution will be deemed to be in compliance if

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[91] *See* 31 C.F.R. §§ 1020.310, 1020.320.

[92] *See* § 1:4[4][b].

[93] 31 U.S.C.A. § 5318(h).

[94] 31 U.S.C.A. § 5312(a)(2) and (c).

[95] *See* 67 Fed. Reg. 21,110, at 21,111 (Apr. 29, 2002) (FinCEN commentary to interim final rule).

[96] *See* § 1:4[i][g].

it is in compliance with its federal financial regulator's existing requirements regarding anti-money laundering programs.[97] United States branches, agencies, and representative offices of foreign banks, as well as Edge Act and agreement corporations, must adopt AML programs that contain the following:

(1) a system of internal controls to assure ongoing compliance;
(2) provisions for independent compliance testing to be conducted by bank personnel or an outside party;
(3) a designated individual to serve as compliance officer; and
(4) training for appropriate personnel.[98]

The compliance program must be in writing, approved by the institution's board of directors, and noted in the minutes.[99] Like other financial institutions, foreign banks subject to the rule were required to implement their anti-money laundering programs by July 24, 2002.[100]

The Federal Reserve Board recently issued a regulation clarifying how the board of directors' approval requirement would apply for state-chartered branches and agencies, as well as for any representative offices. The rule provides that the AML program must be either: (1) approved by the foreign bank's board of directors (that is, the board of directors in the home office) or (2) approved by a delegate acting under the express authority of the board of directors to approve the BSA compliance program.[101] This regulation does not apply to federal branches and agencies of foreign banks, which presumably remain subject to the general OCC rule that "any provision in law, regulation, policy, or procedure that requires a national bank to obtain the approval of its board of directors will be deemed to require a Federal branch or agency to

[97] 31 C.F.R. § 1020.210; *see* 12 C.F.R. § 208.63 (Federal Reserve Board anti-money laundering regulations).

[98] 12 C.F.R. §§ 21.21(c) (OCC), 208.63(c) (Federal Reserve Board). *See also* 12 C.F.R. §§ 211.24(j)(1) (imposing AML program requirement on state branches and agencies, representative offices, cross-referencing 208.63(c)), 211.5(m)(1) (imposing AML program requirement on Edge Act and agreement corporations, cross-referencing 208.63(c)).

[99] 12 C.F.R. § 208.63(b).

[100] Although the final rule did not become effective until October 28, 2002, financial institutions were required to implement their anti-money laundering programs prior to that date on the basis of interim guidance and existing federal regulations on the subject.

[101] 12 C.F.R. § 211.24(j)(1); International Banking Operations, 71 Fed. Reg. 13,934, 13,935 (Mar. 20, 2006).

obtain the approval of parent foreign bank senior management."[102]

[b] Requirements for Correspondent Accounts with Foreign Banks

Section 312 of the USA PATRIOT Act and its implementing Treasury regulation[103] impose requirements with respect to foreign correspondent accounts. The impact of these requirements is not limited to U.S. banks with foreign offices. Rather, Section 312 extends the regulatory reach of the U.S. government to any foreign financial institution that maintains a regular business relationship with a United States financial institution.

[i] Scope of the Rule

The definitions in the correspondent account regulation reflect its broad scope. The rule imposes obligations on any "covered financial institution," which includes not only U.S. banking institutions but broker-dealers, futures commission merchants/introducing brokers, and mutual funds.[104] U.S. offices of foreign banks are treated as U.S. banks for these purposes.[105]

A "correspondent account" is defined as any account "established for a foreign financial institution to receive deposits from, or to make payments or other disbursements on behalf of, the foreign financial institution, *or to handle other financial transactions related to such foreign financial institution*."[106] This last clause extends the coverage of the rule to business relationships

[102] 12 C.F.R. § 28.13(a)(2).

[103] 31 C.F.R. §§ 1020.610, 1020.630, 1020.670.

[104] 31 C.F.R. § 1010.605(e). For purposes of the due diligence regulation, 31 C.F.R. § 1010.610, "covered financial institution" means (i) an insured bank (as defined in the Federal Deposit Insurance Act (FDI Act)); (ii) a commercial bank; (iii) an agency or branch of a foreign bank in the United States; (iv) a federally insured credit union; (v) a savings association; (vi) an Edge Act Corporation; (vii) a trust bank or trust company that is federally regulated and is subject to an anti-money laundering program requirement; (viii) a registered broker-dealer (except persons who register pursuant to Section 15(b)(11) of the Securities Exchange Act of 1934); (ix) a registered futures commission merchant or introducing broker (except persons who register pursuant to Section 4(f)(a)(2) of the Commodity Exchange Act); and (x) a mutual fund. For purposes of the shell bank prohibition, certification requirement, and subpoena provision, "covered financial institution" means (i) an insured bank; (ii) a commercial bank or trust company; (iii) a private banker; (iv) an agency or branch of a foreign bank in the United States; (v) a credit union; (vi) a savings association; (vii) an Edge Act Corporation; and (viii) a registered broker-dealer (except persons who register pursuant to Section 15(b)(11) of the 1934 Act).

[105] 31 C.F.R. § 1010.605(e)(1)(3).

[106] 31 C.F.R. § 1010.605(c).

that would not be considered correspondent accounts in the ordinary sense of the word. An account for purposes of this rule includes "[a]ny formal banking or business relationship established by a bank to provide regular services, dealings, and other financial transactions."[107] This includes not only transaction, asset, and credit accounts but also other types of business relationships not ordinarily thought of as "accounts." For example, an agreement between the U.S. office of a foreign bank and a foreign affiliate to manage U.S. equity portfolios for the foreign affiliate's customers would be deemed a correspondent account under this rule.

The correspondent account rules impose two basic requirements. First, they require covered financial institutions to conduct due diligence on foreign financial institutions for which they maintain correspondent accounts. For purposes of this provision, "foreign financial institution" includes foreign banks; foreign offices of U.S. covered financial institutions; persons organized under foreign law that would be a broker-dealer, futures commission merchant, introducing broker in commodities, or mutual fund if they were located in the United States; and persons organized under foreign law that are engaged in the business of, or readily identifiable as, currency dealers or money transmitters unless such activities are only incidental to their business.[108]

The second provision prohibits U.S. financial institutions from maintaining correspondent accounts for foreign shell banks and requires them to collect certain certifications from foreign correspondent banks. This provision applies only to foreign banks, not other foreign financial institutions. "Foreign bank" is defined as "[a] bank organized under foreign law, or an agency, branch or office located outside the United States of a bank. The term does not include an agent, agency, branch or office within the United States of a bank organized under foreign law."[109]

[ii] Basic Due Diligence

The correspondent account regulations require each covered financial institution to establish a risk-based due diligence program reasonably designed to detect and report, on an ongoing basis, any known or suspected money laundering activity conducted through or involving any foreign correspondent

[107] 31 C.F.R. § 1010.605(c)(2)(i)(A).

[108] 31 C.F.R. § 1010.605(f).

[109] 31 C.F.R. § 1010.100(u).

account.[110] The program must be part of the covered financial institution's overall AML program. Since the procedures must be risk-based, the first step toward complying with this requirement is to assess the risk presented by each foreign financial institution for which the covered financial institution maintains an account.[111] The covered financial institution must then apply "risk-based procedures and controls to each correspondent account reasonably designed to detect and report known or suspected money laundering activity, including a periodic review of the account activity sufficient to determine consistency with information obtained about the type, purpose, and anticipated activity of the account."[112]

[iii] Enhanced Due Diligence

IMLA requires that correspondent accounts for certain foreign banks receive enhanced due diligence. By statute, enhanced due diligence applies to foreign banks that are operating under: (1) an offshore banking license, (2) a banking license issued by a country "designated . . . as noncooperative with international anti-money laundering principles or procedures by an intergovernmental group or organization of which the United States is a member, with which designation the United States representative to the group or organization concurs," or (3) a banking license issued by a foreign country that is subject to special measures.[113] However, U.S. bank regulators have suggested that covered financial institutions should also apply heightened scrutiny to foreign banks deemed high risk by the institution's risk assessment.[114]

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[110] 31 C.F.R. § 1010.610(a).

[111] *See* 31 C.F.R. § 1010.610(a)(2). Factors may include:

1. The nature of the foreign institution's business and the markets it serves;
2. The type, purpose, and anticipated activity of the account;
3. The nature and duration of the U.S. institution's relationship with the foreign institution (and any of its affiliates);
4. The AML and supervisory regime of the foreign institution's jurisdiction and the jurisdiction of the foreign institution's parent; and
5. Information known or reasonably available to the U.S. institution about the foreign institution's AML record.

[112] 31 C.F.R. § 1010.610(a)(3).

[113] 31 U.S.C.A. § 5318(i)(2)(A).

[114] Federal Financial Institutions Examination Council, Bank Secrecy Act/Anti-Money Laundering Examination Manual at 123 (2010) (FFIEC Manual).

The final regulations[115] require covered financial institutions to apply enhanced due diligence as provided by the statute, which includes:

1. If the foreign bank is not publicly traded, ascertaining the identity of each of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner;
2. Conducting enhanced scrutiny[116] of the account to guard against money laundering and report any suspicious transactions; and
3. Ascertaining whether the foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related basic due diligence information.[117]

[iv] Foreign Shell Banks

In addition to the due diligence requirements, IMLA also prohibits covered financial institutions from maintaining correspondent accounts for foreign shell banks.[118] A foreign shell bank is a foreign bank that has no physical presence in any country.[119] The regulation exempts from the prohibition so-called "regulated affiliates," which are shell banks that are affiliated with a nonshell bank and regulated by the same authority that regulates such nonshell bank.[120]

[v] The Certification Process

The regulation also requires each covered financial institution to gather certain information from its foreign correspondent

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[115] *See* Special Due Diligence Programs for Certain Foreign Accounts, 72 Fed. Reg. 44768 (Aug. 9, 2007).

[116] Enhanced scrutiny may include (a) obtaining and considering information relating to the foreign bank's anti-money laundering program to assess the risk of money laundering presented by the foreign bank's correspondent account; (b) monitoring transactions to, from, or through the correspondent account in a manner reasonably designed to detect money laundering and suspicious activity; or (c) obtaining information from the foreign bank about the identity of any person with authority to direct transactions through any correspondent account that is a payable through account and the sources and the beneficial owner of funds or other assets in the payable through account. *See* FFIEC Manual 123.

[117] 31 U.S.C.A. § 5318(i)(2)(B).

[118] 31 U.S.C.A. § 5318(j).

[119] 31 C.F.R. § 1010.605(g).

[120] 31 C.F.R. §§ 1010.605(n), 1010.630(a)(1)(iii).

banks.[121] Although the rule does not specify a single method to comply with this requirement, it provides a safe harbor for reliance upon a certification form published by Treasury and prepared by the foreign bank.[122] The form requires the foreign bank to: (1) certify that it is not a shell bank; (2) certify that it will not use the correspondent account indirectly to provide banking services to a shell bank; (3) identify its shareholders if the bank is not publicly traded; and (4) identify an agent in the U.S. to accept service of process.[123]

Covered financial institutions do not have rigorous verification obligations regarding the information provided in the certification. They are required only to ascertain that all required information has been submitted and that it is not internally inconsistent. However, if a covered financial institution knows or has reason to suspect that any of the information is untrue, it must request the foreign bank to verify or correct the information or take other "appropriate measures" to verify the suspicious information.[124]

[vi] Subpoenas and Enforcement

The Secretary of the Treasury or the U.S. Attorney General may issue a subpoena or summons to any foreign bank that maintains a correspondent account in the U.S. to obtain records relating to its relationship with the U.S. financial institution, including records maintained abroad, or to obtain records relating to the deposit of funds into the foreign bank.[125] If the foreign bank fails to comply with the subpoena or fails to initiate proceedings to contest that subpoena, the Secretary of the Treasury or the U.S. Attorney General (after consultations with each other) may, by written notice, direct the U.S. bank to terminate its relationship with the foreign bank.[126]

Covered financial institutions have their own obligations to enforce compliance with the foreign correspondent account rules.

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[121]The regulation requires each covered financial institution to maintain records in the United States identifying the owners of each foreign correspondent bank whose shares are not publicly traded and the name and street address of a person who resides in the United States and is authorized and has agreed to be an agent to accept service of legal process for records regarding each such account. 31 C.F.R. § 1010.630(a)(2).

[122]31 C.F.R. § 1010.630(b).

[123]*See* FinCEN Certification and Recertification Regarding Correspondent Accounts for Foreign Banks, OMB Control No. 1506-0043.

[124]31 C.F.R. § 1010.630(c).

[125]31 U.S.C.A. § 5318(k)(3); 31 C.F.R. § 1010.670.

[126]31 U.S.C.A. § 5318(k)(3); 31 C.F.R. § 1010.670(d).

Their compliance programs must contain procedures to be followed when the required due diligence cannot be performed, including closing the account where appropriate.[127] They also must freeze and close accounts if certifications are not received within specific timeframes or if a foreign bank fails to reverify suspect information.[128]

[c] Sharing of Information

IMLA also imposes rules concerning the sharing of information between covered financial institutions and U.S. law-enforcement authorities, as well as among covered financial institutions and associations of covered financial institutions. Upon receipt of a request for information from FinCEN, a covered financial institution must "expeditiously" search its records and provide responsive information and records to FinCEN as well as identify a contact person for follow-up requests.[129] Unless otherwise specified, the financial institution need only search for records pertaining to current accounts of each named suspect or accounts maintained within the past 12 months, as well as any transaction or transmission of funds by or on behalf of the named suspect within the past six months.[130] The regulations also establish parameters for the voluntary sharing of anti-money laundering and anti-terrorism information among covered financial institutions and their associations, including a safe harbor from liability for such information sharing.[131]

[d] Other IMLA Requirements

[i] Customer Identification Programs

Treasury Department regulations issued pursuant to Section 326 of the USA PATRIOT Act require every bank, including branches and agencies of foreign banks, to implement a written Customer Identification Program (CIP) "appropriate for its size and type of business[.]"[132] The purpose of the CIP is to "enable the bank to form a reasonable belief that it knows the true

[127] 31 C.F.R. § 1010.630(d).

[128] 31 C.F.R. § 1010.630(d).

[129] 31 C.F.R. § 1010.520(b)(3)(i).

[130] 31 C.F.R. § 1010.520(b)(3)(i).

[131] 31 C.F.R. § 1010.540. To participate, a financial institution or association must file a brief annual notice with FinCEN (a separate notice is not required for each instance of sharing) and verify that its counterpart has done so as well. 31 C.F.R. § 1010.540(b)(2).

[132] 31 C.F.R. § 1010.220(a)(1).

identity of each customer."[133] The CIP procedures "must be based on the bank's assessment of the relevant risks, including those presented by the various types of accounts maintained by the bank, the various methods of opening accounts provided by the bank, the various types of identifying information available, and the bank's size, location, and customer base."[134]

Each CIP must contain certain minimum information collection and identity verification procedures dictated by the regulation.[135] First, a bank must collect from each customer that opens a new account the customer's name, date of birth (for an individual), address,[136] and identification number.[137] After collecting the information, the bank will subject each customer to an identity verification procedure.[138] This procedure may be documentary or nondocumentary. Documentary verification involves examining certain identity documents. For an individual, the bank should almost always demand an "unexpired government-issued identification evidencing nationality or residence and bearing a photograph or similar safeguard, such as a driver's license or passport."[139] For an entity, the bank should generally examine "documents showing the existence of the entity, such as certified

[133] 31 C.F.R. § 1010.220(a)(2).

[134] 31 C.F.R. § 1010.220(a)(2).

[135] *See* 31 C.F.R. § 1010.220(a)(2)(i).

[136] The address must be: (i) for an individual, a residential or business street address; (ii) for an individual who does not have a residential or business street address, an Army Post Office or Fleet Post Office box number, or the residential or business street address of next of kin or of another contact individual; or (iii) for a person other than an individual (such as a corporation, partnership, or trust), a principal place of business, local office, or other physical location. 31 C.F.R. § 1010.220(a)(2)(i)(A)(3). A civilian post office box is not acceptable.

[137] The identification number must be: (i) for a U.S. person, a taxpayer identification number; or (ii) for a non-U.S. person, one or more of the following: a taxpayer identification number; passport number and country of issuance; alien identification card number; or number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard. 31 C.F.R. § 1010.220(a)(2)(i)(A)(4). When opening an account for a foreign business or enterprise that does not have an identification number, the bank must request alternative government-issued documentation certifying the existence of the business or enterprise. 31 C.F.R. § 1010.220(a)(2)(i)(A)(4)(ii) note. A bank may open an account for a customer that has applied for, but has not received, a taxpayer identification number, provided that the bank confirms that the application was filed before the customer opens the account, and obtains the taxpayer identification number within a reasonable period of time after the account is opened.

[138] *See* 31 C.F.R. § 1010.220(a)(2)(ii).

[139] 31 C.F.R. § 1010.220(a)(2)(ii)(A)(1).

articles of incorporation, a government-issued business license, a partnership agreement, or trust instrument."[140] Nondocumentary verification, on the other hand, "may include contacting a customer; independently verifying the customer's identity through the comparison of information provided by the customer with information obtained from a consumer reporting agency, public database, or other source; checking references with other financial institutions; [or] obtaining a financial statement."[141] Documentary verification is the most common practice among domestic banks.[142] Although nondocumentary verification can serve as an alternative to documentary verification, it is often used to supplement rather than supplant the latter, particularly in high-risk or nonface-to-face transactions.

The CIP aims to verify the identity of the bank's "customer," which is defined as "a person that opens a new account."[143] Where the account is opened in the name of an entity, it is the entity—rather than its principals, investors, or employees—that is deemed to be the "customer" for purposes of CIP.[144] However, based on the bank's risk assessment, it may in certain cases ap-

[140] 31 C.F.R. § 1010.220(a)(2)(ii)(A)(2).

[141] 31 C.F.R. § 1010.220(a)(2)(ii)(B)(1).

[142] Although the rule appears flexible on its face, the bank regulators have stated that it "reflects the federal banking agencies' expectations that banks will review an unexpired government-issued form of identification for most customers." FFIEC Manual at 55.

[143] 31 C.F.R. § 1020.100(c)(1)(i). The term "customer" also includes an individual who opens a new account for another individual who lacks legal capacity or for an entity that is not a legal person. 31 C.F.R. § 1020.100(c)(1)(ii). On the other hand, the following persons are excluded from the definition of customer and are therefore exempt from CIP: (1) a person that has an existing account with the bank provided that the bank has a reasonable belief that it knows the person's true identity; (2) a financial institution regulated by a federal functional regulator; (3) a bank regulated by a state bank regulator; (4) a department or agency of the United States, of any state, or of any political subdivision of any state; (5) any entity established under the laws of the United States, of any state, or of any political subdivision of any state, or under an interstate compact between two or more states, that exercises governmental authority on behalf of the United States or any such state or political subdivision; or (6) any entity, other than a bank, whose common stock or analogous equity interests are listed on the New York Stock Exchange or the American Stock Exchange, or whose common stock or analogous equity interests have been designated as a NASDAQ National Market Security listed on the NASDAQ Stock Market (except stock or interests listed under the separate "Nasdaq Small-Cap Issues" heading). *See* 31 C.F.R. §§ 1020.100(c), 1020.315(b).

[144] *See* Customer Identification Programs for Banks, Savings Associations, Credit Unions, and Certain Non-Federally Regulated Banks, 68 Fed. Reg. 25,090, 25,094 (May 9, 2003).

ply its CIP to individuals with authority or control over an entity's account, including signatories.[145] Also, even if the bank applies its CIP only to the entity customer, it still may seek information about principals, investors, or employees in connection with its customer due diligence efforts.

The rule defines "account" as "a formal banking relationship established to provide or engage in services, dealings, or other financial transactions including a deposit account, a transaction or asset account, a credit account or other extension of credit. 'Account' also includes a relationship established to provide a safety deposit box or other safekeeping services, or cash management, custodian, and trust services."[146] Although this definition is slightly narrower than the definition "account" in the foreign correspondent account rule (formal banking relationship vs. formal banking or business relationship), the CIP rules apply to relationships that traditionally have not been viewed as "bank accounts" in the conventional sense of the word such as credit facilities and swap agreements.

The rule requires banks to notify their customers of the CIP procedures to which the customers are subject.[147] Banks often incorporate such notices into customer agreements, particularly in the commercial setting.

[ii] Private Banking Accounts

Section 312 of the USA PATRIOT Act, which contains the foreign correspondent account requirements, also requires banks (including branches and agencies of foreign banks) to perform due diligence on certain "private banking accounts" held for non-United States persons.[148] The Treasury regulation requires banks to maintain a due diligence program that includes policies, procedures, and controls that are reasonably designed to detect and report any known or suspected money laundering or suspicious activity conducted through or involving any private bank-

[145] *See* 31 C.F.R. § 1020.220(a)(2)(ii)(C).

[146] 31 C.F.R. § 1020.100(a)(1). The term "account" does not include: (i) a product or service where a formal banking relationship is not established with a person, such as check-cashing, wire transfer, or sale of a check or money order; (ii) an account that the bank acquires through an acquisition, merger, purchase of assets, or assumption of liabilities; or (iii) an account opened for the purpose of participating in an employee benefit plan established under the Employee Retirement Income Security Act of 1974. 31 C.F.R. § 1020.100(a)(2).

[147] 31 C.F.R. § 1020.220(a)(5)(i).

[148] A "non-U.S. person" is a natural person who is neither a U.S. citizen nor accorded the privilege of residing permanently in the U.S. pursuant to Title 8 of the U.S. Code. 31 C.F.R. § 1010.605(h).

ing account that is established, maintained, administered, or managed in the United States by the bank.[149] This due-diligence program must be part of the bank's anti-money laundering program.[150]

"Private banking account"[151] means an account (or any combination of accounts) maintained at the bank that:

1. Requires a minimum aggregate deposit of funds or other assets of not less than $1 million;
2. Is established on behalf of or for the benefit of one or more non-United States persons who are direct or beneficial owners of the account; and
3. Is assigned to, or is administered or managed by, in whole or in part, an officer, employee, or agent of the bank acting as a liaison between the bank and the direct or beneficial owner of the account.[152]

A beneficial owner of an account is an individual who has a level of control over, or entitlement to, the funds or assets in the account that, as a practical matter, enables the individual, directly or indirectly, to control, manage, or direct the account.[153] The ability to fund the account or the entitlement to the funds of the account alone, however, without any corresponding authority to control, manage, or direct the account (such as in the case of a minor child beneficiary), does not cause the individual to be a beneficial owner.[154]

The due diligence program must be designed to ensure, at minimum, that the bank takes reasonable steps to:

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[149] 31 C.F.R. § 1010.620(a).

[150] 31 C.F.R. § 1010.620(a).

[151] 31 C.F.R. § 1010.605(m). The specific rules discussed in this section apply only to a narrowly defined set of private banking accounts controlled by non-United States persons. More generally, however, private banking involves providing personalized services to high net worth customers. The FFIEC Manual contains specific guidance regarding AML risk assessment and mitigation for private banking in the broader sense of the word. *See* FFIEC Manual at 279 to 285. *See also* Special Due Diligence for Certain Foreign Accounts, 71 Fed. Reg. 492, 505 n.49 (Jan. 4, 2006) (stating that although Section 312 "applies to those private banking accounts meeting the definition in the rule, many covered financial institutions offer forms of private banking relationships that should be given a greater level of due diligence under the institution's risk-based anti-money laundering program than that generally afforded the institution's retail customers").

[152] 31 C.F.R. § 1010.605(m).

[153] 31 C.F.R. § 1010.605(a).

[154] 31 C.F.R. § 1010.605(a).

1. Ascertain the identity of all nominal and beneficial owners of a private banking account.
2. Ascertain whether any of the nominal or beneficial owners of the private banking account is a senior foreign political figure.[155]
3. Ascertain the source of funds deposited into a private banking account and the purpose and expected use of the account.
4. Review the activity of the account to ensure that it is consistent with the information obtained about the client's source of funds, and with the stated purpose and expected use of the account, as needed to guard against money laundering, and to report, in accordance with applicable law and regulation, any known or suspected money laundering or suspicious activity conducted to, from, or through a private banking account.[156]

The due diligence program must also include procedures to be followed in circumstances in which the bank cannot perform appropriate due diligence with respect to a private banking account. These procedures should address when the bank should refuse to open the account, suspend transaction activity, file a SAR, or close the account.[157]

As noted, the measures described in the previous item are only the *minimum* due diligence requirements for accounts covered by Section 312. The nature and extent of any additional due diligence would depend on the bank's risk rating of the account. Examples of potential risk factors involving the client or the

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[155] The term "senior foreign political figure" includes:

1. A current or former senior political figure defined as any:
   a. Senior official in the executive, legislative, administrative, military, or judicial branches of a foreign government (whether elected or not);
   b. Senior official of a major foreign political party; or
   c. Senior executive of a foreign government-owned commercial enterprise.
2. A corporation, business, or other entity that has been formed by, or for the benefit of, any senior political figure.
3. An immediate family member of any senior political figure. "Immediate family member" means spouses, parents, siblings, children, and a spouse's parents and siblings.
4. A person who is widely and publicly known (or is actually known by the bank) to be a close associate of a senior political figure. 31 C.F.R. § 1010.605(p).

[156] 31 C.F.R. § 1010.620(b).

[157] 31 C.F.R. § 1010.620(d).

nominal or beneficial owner of the account include:

1. Lack of a preexisting relationship with the bank;
2. Connection to a jurisdiction with weak AML controls;
3. Involvement in a line of business that is substantially currency based;
4. The relatively large size of the account; and
5. The bank's receipt of information that casts doubt on previous information obtained about the client.[158]

If one of the nominal or beneficial owners of a private banking account is a senior foreign political figure (SFPF), the bank's due diligence program must include enhanced scrutiny of the account that is reasonably designed to detect and report transactions that may involve the proceeds of foreign corruption. Proceeds of foreign corruption are any asset or property that is acquired by, through, or on behalf of a politically exposed person through misappropriation, theft, or embezzlement of public funds, through unlawful conversion of property of a foreign government, or through acts of bribery or extortion, and includes any other property into which any such assets have been transformed or converted.[159]

The scrutiny of accounts of senior foreign political figures should be risk-based. Possible steps may include consulting publicly available information regarding the client's home country, contacting the bank's or affiliated offices operating in the client's home country, and conducting greater than usual scrutiny of the client's employment history and sources of income. The due diligence may uncover information that raises suspicions of political corruption and justifies higher scrutiny of the client's account activity.[160]

As noted in Section 1:2[6][d][iii], banks must establish policies, procedures, and controls that include reasonable steps to ascertain the status of an individual as a senior foreign political figure. The bank should obtain information regarding the client's employment and other sources of income and should inquire directly about the client's SFPF status. The bank should also review public sources of information regarding the client and may check the client's references as well. The regulators recognize that the bank may not be able to identify every single account whose beneficial owner is a SFPF. However, they expect the bank to have reasonable procedures to make such a

[158] *See* FFIEC Manual at 132.

[159] 31 C.F.R. § 1010.620(c).

[160] *See* FFIEC Manual at 133.

determination.[161]

[e] The FFIEC BSA/AML Examination Manual

The BSA and its implementing regulation form only the foundation of the AML compliance obligations of U.S. banking institutions, including branches and agencies of foreign banks. U.S. bank regulators also have imposed a host of specific compliance obligations through supervisory guidance. The central document embodying such guidance is the Federal Financial Institutions Examination Council's BSA/AML Examination Manual (FFIEC Manual). The FFIEC Manual, which at the time of this writing stands at 333 pages plus 19 appendices, is used by examiners to evaluate a bank's compliance with its AML obligations and is, for all practical purposes, just as binding as Treasury's BSA regulations (if somewhat more flexible in its application). Parts of the FFIEC Manual are simply elaborations of existing statutes and regulations. However, the substantial portion of the manual consists of AML safeguards devised entirely by the supervisory agencies or only remotely derived from blackletter law.[162]

The principal supervisory innovations in the FFIEC Manual are: (1) the requirement that banks perform an AML risk assessment, (2) the requirement that banks perform due diligence on customers beyond the identity verification required by the CIP regulations, and (3) the requirement that banks actively monitor transactions for suspicious activity.

[i] Risk Assessment

Bank regulators expect each institution to assess the AML risks presented by its activities.[163] Institutions are also expected to assign a rating to each customer reflecting the risk that a particular customer might conduct money laundering, terrorist

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[161] *See* FFIEC Manual at 134.

[162] To the extent there is a legal basis for these requirements, it potentially rests on the requirement that a bank file a SAR whenever it "knows, suspects, or *has reason to suspect*" that certain conditions exist. 31 C.F.R. § 103.18(a)(2) (emphasis added). This objective standard for reporting means that a bank could be held liable for failure to report suspicious activity even if no one at the bank actually knew or suspected the activity was occurring or was suspicious. In order to guard against this risk, banks must monitor customer transactions for any unusual activity. However, it is difficult to identify unusual activity without knowing enough about the customer to predict the types of transactions in which the customer would normally be expected to engage. Banks gain such knowledge through the CDD process. Risk assessments facilitate efficient CDD and suspicious activity monitoring by enabling banks to focus resources on activities that pose the highest AML risks.

[163] *See generally* FFIEC Manual at 22 to 31.

financing, or other financial crime through the institution. Bank regulators have issued guidance discussing the risks posed by various products, locations, and customer types.[164] That guidance is far too extensive to review here in full. However, as might be expected, common risk factors cited include frequent currency transactions, wire transfers, and international transactions, particularly with offshore financial centers and other "high-risk" jurisdictions.

An institution's overall risk assessment should guide the development of its AML program. Individual customer risk assessment should also be used to determine which accounts merit additional scrutiny. If a bank rates a customer or account as "high risk," the institution will be expected to conduct more extensive due diligence about the customer upon opening the account and to monitor the account more closely for suspicious activities.[165]

[ii] Customer Due Diligence

Banks also are required to subject each customer to a customer due diligence process (CDD) that may involve collection of a great deal more information than was gathered for purposes of the CIP. As noted in Section 1:2[6][d][i], the purpose of CIP is to verify the identity of the customer. The principal goals of CDD, on the other hand, are:

1. To enable the bank to predict the types of transactions in which a customer is likely to engage, thus facilitating the identification of suspicious activities;
2. To provide the bank with sufficient information to assign the customer a risk rating that will guide subsequent due diligence and monitoring; and
3. To identify potential customers for which the risk posed by their activities, backgrounds, or sources of wealth outweigh the benefit of initiating or continuing a business relationship with them.

There are no specific elements that a CDD program must contain. Each bank has been left to devise its own CDD program based on a mix of guidance from regulators, advice from counsel

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[164] *See* FFIEC Manual at 178 to 333.

[165] Banks are expected to use manual or automated transaction monitoring systems to identify suspicious transactions in customer accounts, with special focus on high-risk customers and activities. *See* FFIEC Manual at 67 to 80. They are also required to report certain suspicious activities to the Treasury Department. 31 C.F.R. § 1020.320.

and consultants, and the lessons of its own experience.[166]

[iii] Suspicious Activity Monitoring

While Treasury and banking regulations require banks to report suspicious activity,[167] they do not explicitly require that banks actively monitor for such activity. As a supervisory matter, however, regulators expect banks to use manual or automated transaction monitoring systems to identify suspicious transactions in customer accounts with special focus on high-risk customers and activities.[168] Federal regulators also emphasize the importance of employee education and training in helping to detect money laundering.

[7] The Dodd-Frank Act

On July 21, 2010, President Obama signed the Dodd-Frank Act into law.[169] This major piece of legislation will affect not only U.S. banks, foreign banks, and other traditional financial institutions but also private equity and hedge funds, investment advisers, broker-dealers, "end users" of derivatives, and all public companies. The full impact of the Dodd-Frank Act will not become clear until final rules are adopted in a number of critical areas by a wide range of regulatory agencies, including the Department of the Treasury, the Federal Reserve, Federal Deposit Insurance

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[166] The following is a list of items that regulators have suggested may be appropriate for CDD on high-risk customers:

- Purpose of the account.
- Source of funds and wealth.
- Beneficial owners of the accounts, if applicable.
- Customer's (or beneficial owner's) occupation or type of business.
- Financial statements.
- Banking references.
- Domicile (where the business is organized).
- Proximity of the customer's residence, place of employment, or place of business to the bank.
- Description of the customer's primary trade area and whether international transactions are expected to be routine.
- Description of the business operations, the anticipated volume of currency and total sales, and a list of major customers and suppliers.
- Explanations for changes in account activities.

FFIEC Manual at 65.

[167] In 2010, financial institutions filed almost 700,000 SARs. FinCEN annually publishes an overview of SARs that provides statistics and highlights areas of supervisory concern. *See SAR Activity Review—By the Numbers*, Issue 16 (May 2011).

[168] *See* FFIEC Manual at 71 to 74.

[169] Dodd-Frank Act, Pub. L. No. 111-203 (2010).

Corporation (FDIC), Office of the Comptroller of the Currency, Commodity Futures Trading Commission (CFTC), and Securities and Exchange Commission (SEC).[170]

While Congress did not set out in deliberating and passing the Dodd-Frank Act to alter the financial regulatory landscape for foreign banks in any meaningful fashion, the Act has a number of important provisions that bear on foreign bank operations. While most of those provisions will be discussed in the relevant chapters that follow, this chapter addresses four of the Act's more general provisions affecting foreign banks: regulation of systemically important foreign nonbank financial firms, the Volcker rule enhanced capital standards, and swap activities.

[a] Regulation of Systemically Important Foreign Nonbank Financial Companies

The Dodd-Frank Act establishes a new council of federal and state financial regulators, called the Financial Stability Oversight Council (FSOC), to monitor risks to U.S. financial stability, designate systemically important financial firms for enhanced prudential regulation by the Federal Reserve, and make recommendations to primary financial regulatory agencies to apply new or heightened prudential standards to existing financial institutions or existing financial activities.[171] The Council, by a vote of at least two-thirds of the voting members including an affirmative vote by the Secretary of the Treasury, may designate a "U.S. nonbank financial company"[172] or "foreign nonbank financial company"[173] for supervision and prudential regulation by the Federal Reserve

[170]The Dodd-Frank Act calls for over 250 rulemakings, studies, or other guidance.

[171]*See* Dodd-Frank Act, title 1, subtitle A. The FSOC is to be chaired by the Secretary of the Treasury, and its voting members consist of the Chairman of the Federal Reserve Board of Governors, Comptroller of the Currency, Director of the newly created Bureau of Consumer Financial Protection, Chairman of the SEC, Chairperson of the FDIC, Chairperson of the CFTC, Director of the Federal Housing Finance Agency, Chairman of the National Credit Union Administration Board, and an independent director with insurance expertise appointed by the President. The Council's nonvoting members are the Director of the newly created Office of Financial Research, Director of the newly created Federal Insurance Office, a state insurance commissioner, a state banking supervisor, and a state securities commissioner.

[172]A "U.S. nonbank financial company" is a company incorporated or organized under the laws of the United States or any state that is predominantly engaged in financial activities. A company is "predominantly engaged in financial activities" if (1) the annual gross revenues of the company and all of its subsidiaries from activities that are financial in nature (as defined in Section 4(k) of the BHC Act) represent 85% or more of the company's consolidated an-

if the Council determines that material financial distress at the company, or the activities of the company, could pose a threat to the financial stability of the United States.

In evaluating whether a foreign nonbank financial company could pose a threat to the financial stability of the United States, the Council will consider a number of criteria with respect to the foreign company's U.S. subsidiaries and U.S. operations, including the company's leverage; the extent and nature of the company's off-balance sheet exposures; the company's transactions with other systemically important financial companies; the amount and types of the company's liabilities, including the company's reliance on short-term funding; and any other risk-related factors that the Council deems appropriate.[174] In making a determination, the Council must consult with the company's home-country supervisor.

Foreign nonbank financial companies that are designated by the Council are subject to enhanced prudential standards from the Federal Reserve. These standards may include standards with respect to risk-based capital, leverage limits, liquidity requirements, risk management requirements, resolution plans, credit exposure report requirements, and concentration limits that are more stringent than the standards applicable to financial companies and bank holding companies that do not present similar risks to U.S. financial stability.

The extent to which the Council's designation authority will impact foreign banks currently operating in the United States remains to be seen. However, the Council's designation authority will affect foreign financial companies that transact with foreign banks both inside and outside of the United States.

[b] Volcker Rule

The Volcker Rule, named after former chairman of the Federal Reserve Paul Volcker, amends the Bank Holding Company Act of 1956 to prohibit banks and other banking entities, including

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nual gross revenues, or (2) the consolidated assets of the company and all of its subsidiaries related to activities that are financial in nature (as defined in Section 4(k) of the BHC Act) represent 85% or more of the company's consolidated assets. Dodd-Frank Act, Pub. L. No. 111-203, § 102(a)(4)(B) (2010).

[173] A "foreign nonbank financial company" is a company incorporated or organized in a country other than the United States that is predominantly engaged in, including through a branch in the United States, financial activities. Dodd-Frank Act, Pub. L. No. 111-203, § 102(a)(4)(A) (2010).

[174] Dodd-Frank Act, Pub. L. No. 111-203, § 113(b) (2010).

foreign banks,[175] from engaging in proprietary trading and from sponsoring or investing in private equity or hedge funds.[176] The prohibitions are subject to numerous important exceptions, including for underwriting activities, market-making related activities, risk-mitigating hedging activities, trading in government obligations, trading on behalf of customers, and trading by regulated insurance companies.[177]

Most importantly for foreign banks, the Volcker Rule does not apply to transactions conducted or fund investments made "solely outside of the United States" by an entity that is not directly or indirectly controlled by a banking entity organized under the laws of the United States or of one or more States. Notably, the rule only provides this transaction-based exemption rather than an exemption that applies to all or a portion of foreign banks' activities and potentially places foreign banks in the position of having to determine whether particular transactions conducted outside the United States are within the scope of the rule.

The scope of this exemption, as well as the rule's potential extraterritorial impact in applying to foreign banks with U.S. branches or agencies and such banks' affiliates and subsidiaries (even if such entities do not operate in the U.S.), creates tremendous uncertainty surrounding the Volcker Rule's applicability to foreign banks and their non-U.S. subsidiaries and affiliates. The federal banking agencies are expected to promulgate regulations in 2012 implementing the Volcker Rule, and these regulations may help to determine the specific impact to foreign banks and their non-U.S. subsidiaries and affiliates.[178]

[c] Enhanced Capital Standards

Under the "Collins" amendment to the Dodd-Frank Act,[179] the federal banking regulators are to impose on all depository institu-

[175] The Volcker Rule applies to any insured depository institution, any company that controls an insured depository institution, or that is treated as a bank holding company for purposes of Section 8 of the International Banking Act of 1978, and any affiliate or subsidiary of any such entity. See Dodd-Frank Act, Pub. L. No. 111-203, § 619.

[176] Dodd-Frank Act, Pub. L. No. 111-203, § 619 (2010).

[177] Dodd-Frank Act, Pub. L. No. 111-203, § 619 (2010).

[178] The federal banking agencies issued proposed regulations implementing the Volcker Rule on October 11, 2011. See 76 Fed. Reg. 68846 (Nov. 7, 2011). The proposed regulations requested comment on over 300 questions and issues covering nearly every aspect of the rule.

[179] The "Collins amendment" is named after Senator Susan Collins (R-ME), who advocated for enhanced capital standards throughout Congress's deliberations of the Dodd-Frank Act.

tions and holding companies a generally applicable leverage capital requirement regardless of the size of the institution and not less than those in effect for insured depository institutions on the date of enactment.[180] As part of this statutory mandate of uniform capital requirements across institutions, the special capital rules applicable to bank holding company subsidiaries of foreign banking organizations will no longer apply as of July 20, 2015. These rules have exempted such holding companies from the capital adequacy guidelines provided that their foreign bank parents are well-capitalized and well-managed.[181]

Another important consequences of the Collins amendment is that, following a phase-in period lasting until between 2013 and 2016, "hybrid" capital items like trust preferred securities issued by bank holding companies are no longer eligible for treatment as Tier 1 capital. The enhanced capital standards will have an impact on foreign banks' U.S. operations and may impact the decision whether to conduct banking activities through a U.S. depository institution subsidiary or branch.

[d] Swap Activities

A provision in Dodd-Frank referred to as the "Lincoln amendment"[182] prohibits entities engaged in certain swap activities from receiving federal assistance in the form of access to the Federal Reserve discount window or FDIC deposit insurance. The Lincoln amendment permits insured depository institutions to conduct traditional banking activities and bona fide hedging activities and to move their other swap activities to a separate subsidiary or affiliate without facing such a penalty.[183]

The amendment, however, does not contain a provision similarly permitting foreign banks with an uninsured U.S. branch to conduct traditional banking activities and bona fide hedging activities in the U.S. branch and other swap activities through a separate subsidiary or affiliate. Accordingly, under the plain terms of the new statutory provision, U.S. branches of foreign

[180] Dodd-Frank Act, Pub. L. No. 111-203, § 171 (2010).

[181] *See* Federal Reserve Supervisory Letter SR 01-1 (Jan. 5, 2001).

[182] *See* Dodd-Frank Act, Pub. L. No. 111-203, § 716 (2010). The provisions are named after Senator Blanche Lincoln, former chairman of the Senate Agriculture Committee, who championed them throughout Congress's Dodd-Frank deliberations.

[183] *See* Dodd-Frank Act, Pub. L. No. 111-203, § 716(d) (permitting traditional banking activities and bona fide hedging activities); 716(c) (permitting swap activities to be conducted by an an insured depository institution affiliate that does not receive government assistance).

banks potentially may be asked to forego all government assistance, including access to the discount window, unless they cease swap activities conducted inside such branches and perhaps as well even in separate subsidiaries and affiliates. The absence of a provision permitting foreign banks, like their domestic counterparts, to conduct traditional banking activities and bona fide hedging activities and to move their other swap activities to a separate subsidiary or affiliate was an oversight.[184] Although legislative history clearly establishes that foreign banks' U.S. branches and agencies are to be treated the same as insured depository institutions for purposes of the Lincoln amendment, a legislative correction to the Lincoln amendment may be required to give foreign banks and U.S. regulators certainty that foreign banks in their uninsured branches and agencies may continue to conduct the same swap activities as insured depository institutions and their affiliates.

§ 1:3 Forms of entry and operation

Foreign banks may conduct banking business in the United States through a variety of corporate forms, each having different operational and regulatory consequences. In general, and not surprisingly, the broader the range of banking activities permitted for a given corporate form, the greater the supervisory and regulatory restrictions. As a result, in a number of cases, very specialized corporate forms have developed and proved attractive to foreign banks that have specialized or "niche" business interests in the United States. In other cases, foreign banks have sought to engage in the same broad range of banking activities as would be permissible for a domestic banking organization. In short, the choice of how to enter and operate in the U.S. banking market can be a critical strategic issue for a foreign bank. Accordingly, this part examines and compares the following principal forms for foreign banks to engage in banking business in the United States:

- subsidiary banks;
- branches;

[184] *See* 156 Cong. Rec. S5903 (daily ed. July 15, 2010) (colloquy between Senators Christopher Dodd and Blanche Lincoln) ("[Senator Lincoln] In the rush to complete the conference, there was a significant oversight made in finalizing Section 716 as it relates to the treatment of uninsured U.S. branches and agencies of foreign banks…[Senator Dodd] I agree completely with Senator Lincoln's analysis and with the need to address this issue to ensure that uninsured U.S. branches and agencies of foreign banks are treated the same as insured depository institutions under the provisions of Section 716, including the safe harbor language.").

- agencies;
- representative offices;
- commercial lending companies;
- Edge Act corporations;
- offshore shell branches;
- international banking facilities;
- commercial paper subsidiaries; and
- export trading companies.

[1] Commercial Bank Subsidiaries

Unlike a branch, a U.S. commercial bank subsidiary is a separately capitalized legal entity, the shares of which are owned or controlled by the parent foreign bank. A commercial bank subsidiary of a foreign bank can provide the full range of retail and wholesale banking services available to a domestic bank. Thus, a foreign bank that wishes to engage in retail banking, including by offering federal insurance for deposits, can do so through a subsidiary but generally not through a branch.[185] A commercial subsidiary bank is also the only viable option for a foreign bank to engage in full-service banking in a state that does not permit the establishment of branches or agencies by foreign banks.[186]

As of September 30, 2011, foreign banks had established or acquired 52 commercial bank subsidiaries holding total assets of $1.18 trillion.[187] Of those, 21 were national banks, 30 were state-chartered banks, and one was a federal savings bank.[188] The vast majority were located in New York, New Jersey, California, Florida, or Delaware. Historically, Japanese and British banks were the most active in establishing a retail banking business through U.S. subsidiaries. In recent years, however, Canadian banks have established a significant presence.[189]

To establish or acquire a commercial bank subsidiary in the

[Section 1:3]

[185] As previously noted, there are 10 foreign bank branches that continue to accept FDIC-insured deposits as a result of a grandfather provision in FBSEA. FDIC Institution Directory (as of May 12, 2011), available at http://www.fdic.gov.

[186] Only 29 states and the District of Columbia authorize the establishment of branches by foreign banks.

[187] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[188] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[189] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov. Bank of

U.S., a foreign bank must obtain prior Board approval under Section 3 of the BHC Act.[190] In deciding whether to grant approval, the Board must: (1) determine whether the foreign bank is subject to comprehensive consolidated supervision (CCS) by its home country;[191] (2) determine that the proposed transaction will not substantially lessen competition;[192] and (3) "take into consideration the financial and managerial resources and future prospects of the . . . banks concerned, and the convenience and needs of the community to be served"[193] including the bank's record of performance under the CRA.[194] Furthermore, the Board will assess the foreign bank's capital level to ensure that it is equivalent to that required of a U.S. BHC.[195] A foreign bank also must obtain the approval of the OCC to establish a national bank subsidiary

Montreal has established an extensive retail banking business in the U.S. as Harris Bank. Royal Bank of Canada, Toronto-Dominion Bank, and National Bank of Canada also own U.S. commercial bank subsidiaries.

[190] *See* §§ 6:1 et seq.

[191] 12 U.S.C.A. § 1842(c)(3)(B). In assessing whether a foreign bank is subject to CCS in its home country, the Board considers, among other factors, the extent to which the home-country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; and (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. *See* 12 C.F.R. § 211.24(c). In its orders on applications, the Board has repeatedly stated that these factors are "indicia" of CCS and that "no single factor is essential and other elements may inform the Board's determination." *E.g.*, 89 Fed. Res. Bull. 139 (Apr. 2003) (approving Royal Bank of Canada's acquisition of Admiralty Bancorp Inc.); 85 Fed. Res. Bull. 579, 580 n.6 (Aug. 1999) (approving Piraeus Bank, S.A.'s acquisition of Marathon Banking Corporation and Marathon National Bank); 82 Fed. Res. Bull. 436, 439 (May 1996) (approving Mitsubishi Bank, Ltd.'s acquisition of BHC and its three U.S. subsidiary banks).

[192] 12 U.S.C.A. § 1842(c)(1).

[193] 12 U.S.C.A. § 1842(c)(2).

[194] *See* § 1:2. Under the CRA and related regulations, an insured depository institution has a continuing and affirmative obligation to help meet the credit needs of its local communities, including low- and moderate-income neighborhoods. Regulators take into account an insured institution's CRA performance in evaluating certain types of applications for expansion or acquisition. *See* 12 C.F.R. Pts. 25 (Comptroller), 228 (Board), 345 (FDIC).

[195] *See* 12 C.F.R. § 211.24(c)(2)(ii) (in acting on an application for establishment or acquisition of a U.S. bank subsidiary by a foreign bank, Board may consider the foreign bank's resources, including its current and projected capital

or of the relevant state banking authority to establish a state-chartered bank subsidiary.

Because a subsidiary bank is a separate corporate entity, its operations must be governed by a board of directors. For national bank subsidiaries, the National Bank Act provides that, even with a waiver from the OCC, only a minority of the bank's board of directors may be non-United States citizens.[196] State law citizenship and residency requirements vary, but they also generally require that the board be composed primarily of U.S. citizens and residents.

Operating in the United States through an acquired bank subsidiary enables the foreign bank to offer deposit insurance and therefore provides sources of liquidity not available to uninsured branches and agencies. However, a bank subsidiary requires capitalization separate and apart from its foreign bank parent, and the Collins amendment in Dodd-Frank soon will require capital adequacy from a bank holding company that owns the bank subsidiary and that is owned by the foreign bank.[197]

For these reasons, foreign banks have generally elected to conduct their full service banking operations in the United States through branches instead of bank subsidiaries except where the foreign bank has sought to engage in U.S. retail banking, or acquiring a bank subsidiary was the only way in which the foreign bank was permitted to enter the state. Of course, it is possible for a foreign bank to enter the state both through a branch *and* a bank subsidiary. That may be quite desirable for a foreign bank that seeks to maximize both its retail and wholesale activities. That is, while a bank subsidiary allows the foreign bank to enter retail markets, it is not as efficient a corporate form to engage in wholesale activities as a branch. This is so in part because the amount of a bank's lending to a single borrower (such as a large corporation) is limited by the size of the bank's capital base, which will always be far smaller than the capital

position); The Board of Governors of the Federal Reserve System and the Department of the Treasury, Capital Equivalency Report (June 19, 1992) at 60 (*Capital Equivalency Report*) (establishing guidelines for evaluating capital standards of foreign banks in connection with applications for branches, agencies, and subsidiaries); *1993 Update to the Capital Equivalency Report* (Oct. 1993) (released Sept. 1994). *See also* §§ 2:1 et seq.

[196] 12 U.S.C.A. § 72.

[197] *See supra* § 1.2[7](c).

base of its parent bank.[198] In contrast, the lending limit of a branch is determined by reference to the larger parent bank capital base. Thus, a foreign bank that uses both forms can participate more effectively in both wholesale and retail banking markets while minimizing the total capital required for its overall U.S. banking operations. In addition, U.S. law permits a foreign bank to manage such an arrangement as one integrated business by allocating common business functions, such as data processing and clearing, between the bank and branch.[199]

[2] Branch Offices

The most prevalent form of foreign bank operation in the United States is the branch office. A branch is a legal and operational extension of its parent foreign bank rather than a separately capitalized entity such as a subsidiary bank. However, branches may engage in a broad range of wholesale banking activities. However, branches generally cannot accept retail deposits or offer federal deposit insurance to its depositors. A U.S. branch of a foreign bank is subject to less U.S. regulation than a separately incorporated, federally insured bank subsidiary of a foreign bank.[200] The branch enjoys other advantages as well, such as its parent's larger capital base, that may allow it to borrow with higher credit ratings than a commercial bank subsidiary. The larger capital base also translates into greater capacity for a branch to make loans to a single borrower.

Thus, because most foreign banks choose to focus on wholesale rather than retail activities in the United States, the branch is the corporate form of choice. As of September 30, 2011, there were 196 branches of foreign banks in the United States, accounting for 61.7% of all foreign banking assets in the United States.[201]

The most basic decision facing a foreign bank that wishes to establish a branch in the United States is whether to obtain a federal or state license. The OCC licenses and regulates federal

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[198] As a practical matter, a subsidiary bank can often facilitate compliance with lending limits by selling or participating portions of its credit to its parent foreign bank.

[199] 12 U.S.C.A. § 1843(c)(1) and (8); 12 C.F.R. §§ 225.25(b), 104, 109, 113, 129, 141.

[200] For instance, the branches of foreign banks are in some instances subject to less stringent reserve requirements than those applicable to bank subsidiaries. *See* § 3:2; *see generally* §§ 3:1 et seq.

[201] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

branches and, as is true for national banks, applies a uniform scheme of regulation regardless of the state in which a federal branch is located. As of September 30, 2011, there were 47 federally licensed foreign bank branches operating in the United States.[202] All but six were located in New York and California.[203] Federal branches of foreign banks held a combined total of $197.4 billion in assets.

In contrast, different states have differing licensing and regulatory regimes, but some of them have long experience in regulating foreign branches.[204] Indeed, perhaps for that very reason, state-licensed branches are currently the dominant form of organization for foreign banks. As of September 30, 2011, there were 149 state-licensed branches of foreign banks in the United States[205] with over $1.87 trillion in assets. The vast majority of state-licensed branches are located in New York (95), California (26), Illinois (11), and Florida (8).[206]

There are a number of factors that a foreign bank should consider in deciding whether to establish a federal or state branch, including differences regarding regulatory regimes; authorized entry into a state; permissible activities; branching authority; asset-based requirements; and fiduciary powers. As these factors also constitute basic regulatory issues confronting branches generally, each is discussed in this section.

[a] Regulatory Regime

At the most fundamental level, the decision between a federal or state license constitutes a choice of the primary regulatory authority that will supervise the branch. While the FBSEA established an enhanced role for the Board with respect to all U.S. operations of foreign banks, the licensing authority still plays a substantial on-the-ground supervisory role. Thus, in deciding between a state and federal license (including a choice among different states), a foreign bank should consider the regulator's experience, receptiveness, and reputation with respect

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[202] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[203] As of September 30, 2011, federal branches were located in the following jurisdictions: New York (35), California (7), the District of Columbia (2), and Florida (4).

[204] *See* §§ 4:1 et seq.

[205] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[206] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

to its treatment of foreign banks. If planning to operate in more than one state, a foreign bank should also consider the benefits to be gained by the uniform regulatory scheme applicable to federally licensed banks. Of course, the relationship between the licensing agency and the Board would also be a factor as coordination among regulators has become a very important aspect of foreign bank regulation.[207]

[b] Authorized Entry into a State

In general, a foreign bank may establish a branch in a state by obtaining a license from either the state or the OCC and by also obtaining approval from the Federal Reserve. A State may flatly prohibit such branches, however—as Georgia does[208]—and such a categorical prohibition would be valid with respect to both state *and* federally licensed branches.[209] Conversely, unless a State has flatly prohibited foreign bank entry by legislation, a foreign bank can obtain a *federal* license to operate a branch in that state.[210]

[c] Permissible Activities

A federally licensed branch is generally authorized to engage in the same broad range of banking activities as a national bank.[211] The activities are to be conducted by the branch with the same rights and subject to the same restrictions, penalties, and liabilities as a national bank operating at the same location.[212] Federally licensed branches are subject to different standards, however, if mandated by the IBA such as the prohibition on offer-

[207]Prior to the FBSEA, a foreign bank's decision about where to locate a branch could have had a significant impact on the intensity or frequency of its examinations. Now, however, all federal and state branches and agencies of foreign banks are required to be examined annually by the Board in coordination with the OCC or state regulator. *See* 12 U.S.C.A. §§ 3105(c), 1820(d). As a result, examination standards and frequency are now much more consistent than in the past, which means that the issue of examinations is less likely to influence a foreign bank's choice of license.

[208]Ga. Code Ann. §§ 7-1-710, 7-1-716(e).

[209]12 U.S.C.A. § 3102(a)(1).

[210]12 U.S.C.A. § 3102(a)(1). Twenty-nine states and the District of Columbia have specifically authorized the establishment of branches by foreign banks. Most state-licensed foreign bank branches are chartered in one of four states: New York, California, Illinois, and Florida. *See* Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[211]12 C.F.R. § 28.13(a).

[212]12 C.F.R. § 28.13(a).

ing federally insured or retail deposits.[213] The OCC is authorized to issue opinions, interpretations, or rulings regarding the permissible activities of federally licensed branches.[214]

By contrast, the permissible range of activities of a state branch varies by state.[215] Those states that license branches for foreign banks—some do not—generally authorize them to engage in a broad range of traditional banking activities.[216] (As with federal branches, of course, federal law prohibits state-licensed branches from offering insured or retail deposits.)[217]

A State's authority regarding the permissible activities of state branches is circumscribed by federal law, however. The FBSEA generally limits the activities of a state-licensed branch to those permissible for a federally licensed branch,[218] just as the activities of a state bank are generally limited to those of a national bank.[219] There are exceptions, however. Federal law permits a State to authorize a state-licensed branch to engage in the following activities that are *not* permitted for a federally licensed branch: activities conducted as agent (i.e., real estate brokerage); activities that the FDIC (in the context of federally insured banks) has previously determined do not constitute a "significant risk" to an affected federal deposit insurance fund; activities that the OCC has authorized subject to limits (the state may provide that the limits do not apply); and other activities permitted by the Federal Reserve Board, by application, as "consistent with sound banking practice."[220]

In sum, a State may license foreign branches to engage in a marginally broader range of activities than is permissible for a federal branch—but it may also limit such activities to a nar-

[213] 12 U.S.C.A. § 3104(b); *see* 12 C.F.R. § 28.16.

[214] 12 C.F.R. § 28.13(c). The OCC's authority to issue opinions, interpretations, or rulings regarding federal branches' permissible activities is for the purpose of determining whether state licensed branches may engage in certain types of activities.

[215] *See* § 4:7[1].

[216] *See, e.g.*, N.Y. Banking Law § 202-a.

[217] *See* § 4:7[1]. ("Even if the state did permit the acceptance of retail deposits, federal law prohibits such deposit-taking unless it takes place in a separately chartered subsidiary.").

[218] 12 U.S.C.A. § 3105(h)(1); *see also* § 4:7[1].

[219] 12 U.S.C.A. § 1831a.

[220] 12 C.F.R. § 211.29. If the branch is one of the 10 grandfathered state branches that is federally insured, the foreign bank must indicate in its application that the activity will pose no risk to the deposit insurance fund and provide a copy of the FDIC's approval of the activity. 12 C.F.R. § 211.29(c)(4).

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[d] Authority to Establish Additional Branches

As provided by the Riegle-Neal Act, state- and federally licensed branches operate under essentially the same interstate branching rules.[221] As described previously, that Act and the Dodd-Frank Act eliminated most of the substantial obstacles to interstate banking and branching, and foreign banks enjoy the benefits of the new rules to much the same extent as domestic banks.

Indeed, the new rules basically eliminated the need for so-called "limited branches," which are permissible branch forms for both state and federally licensed branches.[222] A limited branch can generally engage in the same activities as an unrestricted branch except that it cannot accept most domestic deposits.[223] The main advantage of a limited branch is that it is not subject to interstate branching restrictions[224] but that advantage is not as significant in the wake of the changes made by the Riegle-Neal Act and the Dodd-Frank Act. As of September 30, 2011, there were only 30 limited branches of foreign banks, accounting for less than one percent of foreign banking assets in the United States.[225]

While federal law now governs most *inter*state banking and branching activities, state law remains paramount with respect to *intra*state branching. As a result, state law determines whether a foreign bank with a branch in a state may establish additional branches in that state. However, the rules for such intrastate branching can be different for state and federal branches, and the latter could well have greater branching authority in a particular state.

To illustrate, a State is free to adopt a law that limits the abil-

[221] *See* § 1:2[4].

[222] 12 U.S.C.A. § 3103(a)(7)(A). Branches that are limited in this manner are sometimes called "restricted" branches although Regulation K uses the term "limited branch." 12 C.F.R. § 211.21(s).

[223] A limited branch agrees to receive only such deposits as would be permitted to an Edge Act corporation, discussed at § 1:3[6]. *See* 12 U.S.C.A. § 3103(a)(7)(A)(ii). Thus, permissible deposits for a restricted branch are generally limited to deposits from non-U.S. governments, residents, or corporations, as well as certain export-related deposits. *See* § 1:3.

[224] 12 U.S.C.A. § 3103(a)(7).

[225] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov. There were 14 federal restricted branches and 16 state restricted branches.

ity of a state-licensed branch to open additional branches in a state even if a *bank* chartered by that state is permitted to engage in statewide branching. Indeed, some states limit foreign banks to a single branch,[226] and as a practical matter, many foreign banks appear to be content with having only one branch in a state.

However, the same state's rules would apply differently to a federal branch. As a matter of federal law, a foreign bank with a federal branch in a state may establish additional branches to the extent permitted for a national *bank* located in that state.[227] Additionally, a national bank located in a state is permitted by a different provision of federal law to establish additional branches in that state to the extent permitted for a state *bank* in that state.[228] Putting the two federal provisions together, a foreign bank with a federally licensed branch in a state may establish additional branches in that state to the extent permitted for a state bank in that state—even though a foreign bank with a state-licensed branch in that state would be prohibited from establishing *any* additional branches. Thus, a foreign bank that is interested in establishing multiple branches in a single state may prefer a federal license in many states.[229]

[e] Asset Requirements

There are two types of asset-based requirements for branches of foreign banks: (1) asset maintenance requirements, and (2) asset pledge requirements. Asset maintenance provisions require a foreign bank to hold assets of a certain type and in a certain amount at a branch. Asset pledge provisions require a foreign bank to deposit with another bank assets of a certain type and in a certain amount.[230]

Of the two, asset maintenance requirements are less widespread and less of an issue for most foreign banks. With respect

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[226] *See* Glidden and Shockey, U.S. Branches and Agencies of Foreign Banks: A Comparison of the Federal and State Chartering Options, 1980 U. Ill. L. Rev. 65, 82–83.

[227] 12 U.S.C.A. § 3102(h).

[228] 12 U.S.C.A. § 36(c).

[229] However, a foreign bank may not establish both a federally licensed branch and a federal agency in the same state. 12 U.S.C.A. § 3102(e); *accord* N.Y. Banking Law § 202-d (a foreign bank may not establish both a state-licensed branch and agency in New York).

[230] The deposited funds for an asset pledge may not be withdrawn without the bank regulator's prior approval and must be pledged to the regulator. *See, e.g.*, 12 U.S.C.A. § 3102(g); 12 C.F.R. § 28.15.

to federal branches of foreign banks, the OCC does not impose *any* general asset maintenance requirement though it has authority to do so in particular instances.[231] Asset maintenance requirements have been scaled back at the state level as well. New York, for example, has completely eliminated its general asset maintenance requirement for foreign banks.[232]

In contrast, asset pledge requirements continue to be an important consideration for both state- and federally licensed branches. A federally licensed branch must maintain an asset pledge, or "capital equivalency deposit" (CED), equal to at least the minimum capitalization of a national bank in the same location or five percent of the branch's third-party liabilities (liabilities to unrelated persons), whichever is greater.[233] Acceptable instruments for the CED include U.S. government-issued or guaranteed obligations; certain state and local obligations; corporate debt securities and other mortgage-related and small business-related securities that are rated investment grade; certain certificates of deposit payable in the United States; bankers' acceptances payable in the United States; and other assets permitted by the Comptroller.[234] The OCC recently added to the list of acceptable instruments repurchase agreements and dollar deposits payable in any G-10 country.[235]

Notably, the OCC adopted a more flexible approach to the five percent requirement. It amended its regulations to exclude from the base on which the CED is calculated liabilities of an international banking facility (IBF)[236] to third parties and of a federal branch of a foreign bank to an IBF.[237] The OCC may also now exclude liabilities from repurchase agreements on a case-by-

[231] The Comptroller has authority to impose an asset maintenance requirement on federal branches at any time and may do so on both a state-by-state and a case-by-case basis. 12 C.F.R. § 28.20.

[232] *See* N.Y. Comp. Codes R. & Regs. tit. 3, §§ 51.3, 322.1. However, the NYSBD still has authority to impose an asset maintenance requirement on a state-licensed branch or agency on a case-by-case basis. N.Y. Comp. Codes R. & Regs. tit. 3, § 51.3.

[233] *See* 12 U.S.C.A. § 3102(g); 12 C.F.R. § 28.15.

[234] *See* 12 U.S.C.A. §§ 24, 3102(g)(1) to (4); 12 C.F.R. §§ 1.2, 28.15.

[235] Rules, Policies, and Procedures for Corporate Activities; International Banking Activities, 68 Fed. Reg. 70,691, 70,695 to 70,696 (Dec. 19, 2003).

[236] An IBF is essentially a separate set of records operated by a bank's U.S. office, which segregates a matching amount of certain foreign source deposits and foreign loans. *See* 12 C.F.R. § 204.8(a). For a discussion of IBFs, *see* § 1:3[7].

[237] Rules, Policies, and Procedures for Corporate Activities; International Banking Activities, 68 Fed. Reg. 70,691, 70,695 to 70,696 (Dec. 19, 2003).

case basis.[238] In addition to relaxing its approach to calculating the amount of a CED, the OCC also loosened the regulation governing where a foreign branch's CED must be deposited.[239]

These developments were prompted in part by the relaxing of state asset pledge requirements in New York and elsewhere.[240] Moreover, in 2002 the New York State Banking Department (NYSBD) reduced the amount of the required asset pledge from five percent to one percent of third-party liabilities, as well as capped the total required pledge at $100 million for "well rated" banks that meet certain qualifying standards.[241] In addition, New York allows a branch to satisfy the pledge requirement with a wider range of assets than is currently permissible under federal law.[242]

[f] Fiduciary Powers

In general, the fiduciary powers of a federal branch are the same as those of a national bank located in the same state.[243] In turn, a national bank generally may engage in fiduciary activities to the extent permitted for a state-chartered bank of the state where the national bank is located.[244] Thus, a federally licensed branch generally may engage in the same fiduciary activities as a state-chartered bank in the same jurisdiction. By contrast, state-licensed branches often do not have such broad fiduciary powers

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[238] Rules, Policies, and Procedures for Corporate Activities; International Banking Activities, 68 Fed. Reg. 70,691, 70,695 to 70,696 (Dec. 19, 2003).

[239] Rules, Policies, and Procedures for Corporate Activities; International Banking Activities, 68 Fed. Reg. 70,691, 70,695 to 70,696 (Dec. 19, 2003).

[240] *See* OCC News Release, "OCC Reduces Regulatory Burden for Well-Managed Federal Branches" (Mar. 4, 2002), available at http://www.occ.treas.gov (noting that proposed amendment to the statutory CED requirement would "give the Comptroller the same flexibility that states now have" with respect to asset maintenance requirements); *see also* N.Y. Comp. Codes R. & Regs. tit. 3, §§ 322.1, 322.4 (2007). New York requires the greater of (1) one percent of the average total liabilities for the previous month or (2) $2 million.

[241] *See* N.Y. Comp. Codes R. & Regs. tit. 3, §§ 322.1(f), 322.4 (2007).

[242] For instance, the NYSBD permits state-licensed foreign bank branches to pledge highly rated commercial paper and bankers' acceptances to satisfy the requirement. *See* N.Y. Banking Law § 202-b(1); N.Y. Comp. Codes R. & Regs. tit. 3, § 322.2.

[243] 12 U.S.C.A. § 3102(b); 12 C.F.R. § 28.13(a)(1).

[244] 12 U.S.C.A. § 92a(a).

available to them[245] because many states expressly impose stricter limitations on the fiduciary powers of state-licensed branches of foreign banks than on their state-chartered banks.[246] Thus, in certain states a foreign bank interested in exercising fiduciary powers may find a federally licensed branch more attractive than a state-licensed branch.

[3] Agencies

A U.S. agency of a foreign bank is similar to a branch except that it generally may not accept deposits.[247] Like a branch, an agency is a legal and operational extension of the parent bank rather than a separate corporate entity. Agencies engage primarily in corporate and commercial lending and in facilitating international transactions. While it generally cannot accept deposits,[248] an agency is permitted to accept limited credit balances and to fund itself in the U.S. interbank markets.[249] At one time, agencies were subject to less restrictive regulation than branches, but that is generally no longer the case. As of September 30, 2011, foreign banks operated 50 agencies in the United States, accounting for $135.6 billion in assets. All but two were located in Florida (16), New York (15), California (8), or Texas (9).[250]

The establishment of an agency requires the approval of the

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[245]Section 202(a) of FBSEA provides that a state-licensed branch's fiduciary powers may not exceed those permissible for a federally licensed branch. 12 U.S.C.A. § 3105(h)(1).

[246]A notable exception is New York, which generally accords state-licensed branches of foreign banks the full range of fiduciary powers available to domestic state and national banks. New York passed legislation in 1984 that eliminated: (1) the requirement for reciprocity of trust powers for foreign banks' state-licensed branches, *see* 1984 N.Y. Laws ch. 360 §§ 48, 51, (codified at N.Y. Banking Law §§ 201-b, 202-a); (2) the limitation on the types of trust customers permissible for state-licensed branches, 1984 N.Y. Laws ch. 360 § 48 (codified at N.Y. Banking Law § 201-b), and (3) the 10% of capital pledge as a condition for state banks exercising fiduciary powers, 1984 N.Y. Laws ch. 360 § 48.

[247]*Compare* 12 C.F.R. § 211.21(b) and (d).

[248]Some states provide agencies of foreign banks with limited deposit-taking authority such as acceptance of foreign sources deposits or issuance of certain large-denomination obligations. *See* discussion later in this section.

[249]12 U.S.C.A. § 3101(1); 12 C.F.R. § 28.11(h). A credit balance is a deposit-like obligation that is placed for a specific purpose, such as facilitating a specific transaction, and is withdrawn within a reasonable time after the purpose is fulfilled.

[250]Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov. The remaining agencies were located in Georgia and Missouri. New York and California do not allow foreign banks to establish both a branch office and an agency within their jurisdictions, which requires a foreign bank to choose between the

Board and either the OCC or relevant state banking authority, depending on whether it is federally or state-licensed. However, there is currently only one federally licensed agency of a foreign bank,[251] which seems to be the result of two factors: federal agencies have few advantages over federal branches;[252] and some state agencies—notably including those in California, Florida, and New York[253]—have limited deposit-taking authority while federal agencies do not.

Even state-licensed agencies have declined in appeal over time, however. Before FBSEA, a state-licensed agency was subject to fewer regulatory constraints than a branch and, in particular, had more permissive lending limits than branches. Now, however, all agencies and branches are treated the same for lending limit purposes as all loans to a borrower from all state and federal branches and agencies of a foreign bank must be aggregated on a nationwide basis to determine whether the applicable lending limit has been exceeded.[254] As a result, state-licensed agencies no longer enjoy significant advantages over state-licensed branches in most states.[255]

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two. *See* Cal. Fin. Code § 1707; N.Y. Banking Law § 202-d. However, a foreign bank also has the option to conduct business through a bank subsidiary in either state.

[251]Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov (indicating that only Arab Bank, plc maintains a federally licensed U.S. agency). Federal agencies generally are subject to the same regulatory requirements imposed on federal branches. *See* 12 C.F.R. Pt. 28 (1999).

[252]*See* 12 C.F.R. Pt. 28 (federal agencies generally subject to same regulatory requirements imposed on federal branches).

[253]California and Florida allow state-licensed agencies to accept certain foreign source deposits. *See* Cal. Fin. Code § 1755(a)(2); Fla. Admin. Code R. 69U-140.008(6). Similarly, New York allows agencies to accept foreign source deposits and to issue large-denomination obligations, including certificates of deposit, to corporations, partnerships, and unincorporated associations. *See* N.Y. Banking Law § 202-a; N.Y. Comp. Codes R. & Regs. tit. 3, § 323.3.

[254]12 U.S.C.A. § 3105(h)(2); 12 C.F.R. § 211.28(a). In New York, state-licensed agencies are also subject to asset pledge requirements applicable only to branches. *See* N.Y. Banking Law § 202-b(1).

[255]In New York, for example, a report commissioned by the NYSBD proposed phasing out agencies altogether. *See* Report of the Superintendent's Advisory Committee on Transnational Banking Institutions 103–104 (Mar. 1992) (available from the NYSBD) (Heimann Committee Report) (recommending phaseout of agencies if asset pledge requirements are applied to New York agencies). Although New York still licenses agencies, their number has declined from 22 to 11 since 1999.

[4] Representative Offices

A "representative office" is any U.S. office of a foreign bank that is not a branch, agency, or commercial lending company.[256] A representative office may engage only in representational and administrative functions on behalf of a foreign bank, such as business solicitation, research, loan production, liaison between the foreign bank's offices and U.S. correspondent banks, customer relations, and back-office functions.[257] A representative office may not engage in banking activities that may be performed at a branch, agency, or subsidiary bank and generally may not exercise final decision-making power over any banking transaction.[258]

Because a representative office is the simplest form of organization for foreign banks to establish, it is frequently used as the vehicle for a foreign bank's initial entry into the U.S. market. Representative offices are also sometimes used to establish a presence in a jurisdiction that does not permit branches or agencies of foreign banks, potentially in conjunction with a subsidiary bank or Edge Corporation.[259] As of September 30, 2011, foreign banks had established 138 representative offices in 17 states and the District of Columbia.[260]

To establish a representative office or relocate an existing representative office to another state, a foreign bank must obtain prior Board approval.[261] In evaluating an application for a representative office, the Board is authorized, but not required, to consider the same standards applicable to the proposed establishment by foreign banks of branches, agencies, and commercial lending company subsidiaries.[262] The Board has indicated that it will evaluate representative office applications on a case-by-case basis in light of the nature and extent of the office's proposed

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[256] *See* 12 C.F.R. § 211.21(x).

[257] 12 C.F.R. § 211.24(d)(1)(i).

[258] 12 C.F.R. § 211.24(d).

[259] *See* §§ 4:1 et seq.

[260] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov. Most were located in New York (43), Texas (13), California (15), and Florida (12). *See* §§ 4:1 et seq.

[261] 12 U.S.C.A. § 3107; 12 C.F.R. §§ 211.21(2)(5), 211.24(a)(2). The requirement of prior Board approval was added by Section 204 of FBSEA. Previously, a representative office could be established through notice registration to the Treasury.

[262] 12 U.S.C.A. § 3107; 12 C.F.R. § 211.24(d)(2).

activities.[263]

The Board provides expedited procedures for establishing a representative office in certain situations. First, a foreign bank may establish a representative office after 45 days' notice to the Board if (1) the Board has not yet determined the foreign bank to be subject to consolidated comprehensive supervision, but the foreign bank is subject to the BHC Act, either directly or through Section 8(a) of the IBA; (2) the Board previously has approved an application by the foreign bank to establish a branch or agency; or (3) the Board previously has approved an application by the foreign bank to establish a representative office.[264] Second, a foreign bank may operate under "general consent" to establish a representative office if the bank is subject to the BHC Act and *has* previously been found to be subject to consolidated country supervision by its home-country supervisor.[265] Finally, general consent is also available to establish a representative office that engages solely in limited administrative or back-office activities.[266]

Because of their limited powers, representative offices traditionally have not been heavily regulated by state banking authorities. Recently, however, some states have begun to require substantially more information than in the past. For example, New York has revised its licensing regulations for representative offices to require each applicant to provide detailed information concerning its parent bank and the regulatory system in its home country.[267] Representative offices also are subject to examination by state regulators in some jurisdictions[268] though FBSEA makes the

[263] *See* 58 Fed. Reg. 6351 (preamble to final rules).

[264] 12 C.F.R. § 211.24(a)(2)(i). The Board may waive the 45-day period if immediate action is required, or suspend the notice period and require a full application if the notification raises significant policy or supervisory concerns. 12 C.F.R. § 211.24(a)(2)(ii).

[265] 12 C.F.R. § 211.24(a)(3)(i)(A).

[266] 12 C.F.R. § 211.24(a)(3)(i)(C). The activities of this limited administrative or back office (1) must be clearly defined; (2) must be performed only in connection with the U.S. banking activities of the foreign bank; and (3) must not include contact with customers or potential customers beyond incidental contact with existing customers relating to administrative matters. 12 C.F.R. § 211.24(a)(3)(i)(C).

[267] *See* N.Y. Comp. Codes R. & Regs. tit. 3, Supervisory Policy FB 102.3 and 102.6.

[268] For example, California and New York impose licensing and examination requirements for representative offices of foreign banks. *See* Cal. Fin. Code §§ 1700(n), 1710, 1725 to 1729; Cal. Code Regs., tit. 10, §§ 10.13100 to 10.13281; N.Y. Banking Law §§ 221-a, 221-b.

Board the overall federal examiner of such offices.[269] The Board coordinates its examinations of representative offices with the appropriate state and federal supervisors but retains direct oversight to ensure that such offices are not engaging in banking activities.[270] In the event of a violation, the Board has express authority to terminate a representative office.[271]

[5] Commercial Lending Companies

New York authorizes a specialized nondepository lending institution known as an Article XII investment company,[272] which the Federal Reserve Board recognizes in Regulation K as a "commercial lending company."[273] A foreign bank considering only a limited operation in New York may acquire an Article XII investment company after receiving approval from the NYSBD and the Board.[274] As of September 30, 2011, one foreign bank maintained an Article XII investment company.[275] The principal advantage of an Article XII investment company is that it has broad borrowing and lending powers and may also accept credit balances without being subject to Federal Reserve requirements. In addition, overseas firms have also been interested in establishing such companies for tax considerations.

Specifically, an Article XII investment company may engage in (1) borrowing, (2) lending, purchasing, and discounting bills of exchange, notes, and other obligations, (3) transmitting money, (4) holding credit balances, (5) trading coin and bullion, (6) leasing, (7) operating foreign branches where credit balances may be received, and (8) guaranteeing certain obligations of customers. Like an agency, however, an Article XII investment company has

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[269] 12 U.S.C.A. § 3107(c); 12 C.F.R. § 211.26(a)(2). The Board has clarified that FBSEA does not provide the Board with general authority to examine U.S. affiliates of a foreign bank whose only U.S. office is a representative office. *See* 58 Fed. Reg. 6,356.

[270] *See* 58 Fed. Reg. 6,352.

[271] 12 C.F.R. § 211.25.

[272] N.Y. Banking Law §§ 507 to 520.

[273] 12 C.F.R. § 211.21(g).

[274] 12 U.S.C.A. § 3105(d)(1). The application process for Board approval of an Article XII investment company is the same as that for a branch or agency office. 12 C.F.R. § 211.24(a)(1)(B) and (b).

[275] In addition, several large U.S. financial companies also have chartered Article XII investment companies, including American Express, General Electric, and Western Union. New York State Banking Dept., Investment Companies (Article XII), Supervised Institutions (Sept. 6, 2011), available at http://www.banking.state.ny.us.

no general deposit-taking authority.[276]

One disadvantage of an Article XII investment company is that, unlike an agency, it must maintain minimum capital of $2 million.[277] The NYSBD may impose a higher capitalization requirement as a licensing condition on a case-by-case basis.[278]

[6] Edge Act Corporations

Another vehicle that a foreign bank may use to engage in U.S. banking operations is a so-called "Edge Act" corporation, which is a separate corporate entity that is authorized to engage in specified types of international banking activities.[279] Domestic banking organizations use Edge Act corporations to facilitate their international businesses, and such corporations may have operations in the United States that support their overseas activities.[280] Because a foreign bank's business in the United States is often tied to its international activities, the regulatory limits on an Edge Act corporation's activities may not significantly affect the foreign bank's U.S. operations. If that is the case, then at least in the past there have been other advantages to the Edge Act vehicle that some foreign banks have found attractive. Prior approval of the Board is required to establish an Edge Act corporation.[281]

The powers of an Edge Act corporation are similar to those of a wholesale bank except that its activities must generally have an international connection. For instance, an Edge Act corporation may accept certain deposits related to international banking whereas an agency generally is not permitted to accept any deposits.[282] Likewise, the lending powers of an Edge Act corporation generally are restricted to certain international transactions

[276] An Article XII investment company cannot accept deposits of any kind though it can maintain substantial credit balances. N.Y. Banking Law § 509(4). The Board has determined that an Article XII investment company's credit balances are not demand deposits within the meaning of the BHC Act. *See* European American Bancorp, 63 Fed. Res. Bull. 595 (June 1977).

[277] N.Y. Banking Law §§ 509, 4001.

[278] N.Y. Banking Law § 509.

[279] 12 U.S.C.A. §§ 611 to 632. A foreign bank also may establish an "Agreement Corporation," a state-chartered corporation that has entered into an agreement with the Board that it will not exercise any power that is impermissible for an Edge Act corporation. 12 U.S.C.A. § 601.

[280] 12 C.F.R. § 211.6.

[281] 12 U.S.C.A. § 614; 12 C.F.R. § 211.5(a).

[282] 12 C.F.R. § 211.6(a)(1).

set forth in the Board's Regulation K.[283] An Edge Act corporation's other banking and financial powers are restricted generally to those incidental to an international or foreign business.[284]

When compared with a branch or agency, however, an Edge Act Corporation has a number of potential disadvantages including: (1) separate capitalization and capital adequacy requirements; (2) the applicability of lending limits that are based on the corporation's capital as opposed to its parent bank's capital; and (3) significant restrictions on permissible types of extensions of credit.[285] Furthermore, the principal characteristic of Edge Act corporations that attracted foreign banks had been their ability to avoid interstate banking and branching restrictions,[286] but the attractiveness of that characteristic substantially diminished as a result of the Riegle-Neal Act.

Consequently, the number of Edge Act Corporations owned by foreign banks has sharply declined. In 1990, foreign banks operated 23 Edge Act Corporations; by September 30, 2011, that number had declined to just four.[287]

[7] International Banking Facilities

An IBF is simply a separate set of accounting books on which certain types of banking organizations may accept deposits from and make loans to foreign residents and organizations.[288] An IBF can be established by a U.S. bank (including the subsidiary of a

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[283] 12 C.F.R. § 211.6(a)(3). An Edge Act Corporation is limited to engaging in the following credit activities: (1) directly financing: (a) contracts, projects, or activities performed substantially abroad; (b) importation into and exportation from the United States of goods; (c) domestic shipment or temporary storage of imported and exported goods; (d) assembly or repackaging of goods for export or import; or (e) production of goods under order or identifiable as being directly for export; (2) issuing guarantees or letters of credit related to the above extensions of credit; (3) assuming or acquiring participations in extensions of credit an Edge Act Corporation can finance directly; and (4) providing credit and other banking services for both foreign and domestic purposes to foreign governments and agencies, foreign persons, and certain international entities limited to an international business.

[284] For example, an Edge Act Corporation may broker securities or provide investment advisory services, including mergers and acquisition advice, on behalf of both foreign and U.S. customers. In the case of U.S. customers, however, the securities or assets must be foreign. 12 C.F.R. § 211.6(a)(6)(i), (iv), (v).

[285] *See* 12 C.F.R. §§ 211.6, 211.8, and 211.9.

[286] *See* 12 U.S.C.A. § 615(b); 12 C.F.R. § 211.4(c).

[287] Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[288] 12 C.F.R. § 204.8(a).

foreign bank), a U.S. branch or agency of a foreign bank, or a U.S. office of an Edge Act or Agreement Corporation (including one owned by a foreign bank).

The main advantage of an IBF is that its liabilities are not subject to reserve requirements.[289] As a result, funds in an IBF can be used to provide identical banking services at a lower cost. IBF funds are also free from deposit insurance premiums though that advantage is generally not relevant to foreign bank branch or agency operations, which are generally not federally insured.

An IBF may extend credit directly or indirectly to: (1) all bank offices located abroad; (2) Edge Act or Agreement Corporations; (3) U.S. offices of the establishing entity; (4) other IBFs; (5) foreign national governments; (6) certain international organizations; and (7) foreign residents or foreign branches, subsidiaries, or affiliates of U.S. corporations though in this latter case, the funds must be used only to finance the borrower's operations outside the United States.[290] An IBF may accept deposits from the first six types of entities listed in the preceding sentence.[291] In addition, IBFs may accept deposits on slightly different terms from foreign residents and foreign branches, subsidiaries, and affiliates of U.S. corporations.[292] Subject to these international-connection requirements, the authority of an IBF to engage in a particular activity derives from the institution that owns the IBF; thus, for example, if the establishing entity may exercise fiduciary powers or engage in foreign exchange transactions, the IBF generally may do so as well.[293]

To establish an IBF, an eligible institution must notify its District Federal Reserve Bank at least 14 days prior to the first reserve computation period for which it intends to operate the IBF. No prior approval is required.[294] Each reporting entity of a banking institution may establish an IBF.[295]

Because they offer significant benefits without burdensome

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[289] 12 C.F.R. § 204.8(c). Depending on state law, the use of an IBF also may result in tax advantages. For example, New York State and New York City both provide favorable tax treatment to an IBF. *See* §§ 3:1 et seq.

[290] 12 C.F.R. § 204.8(a)(3).

[291] 12 C.F.R. § 204.8(a)(2)(i).

[292] 12 C.F.R. § 204.8(a)(2)(ii). Such deposits must be held at least two business days, and except to close an account, withdrawals must be made in amounts of $100,000 or more.

[293] *See* 46 Fed. Reg. 32,426, at 32,428 (June 23, 1981).

[294] 12 C.F.R. § 204.8(e).

[295] 12 C.F.R. § 204.8(d).

obligations, IBFs have increased dramatically in recent years. Foreign banks, in particular, aggressively use IBFs to reduce the cost of complying with reserve and asset pledge requirements.[296] Indeed, a majority of the agencies, branches, bank subsidiaries, and Edge Act subsidiaries of foreign banks have established IBFs.[297]

[8] Offshore Shell Branches

Many foreign banks maintain offshore branches in the Cayman Islands or other jurisdictions for tax and reserve advantages. These operations are frequently "shell branches" or separate sets of accounting books managed from a U.S. office of the foreign bank. The advantages of an offshore shell branch are less pronounced as a result of the favorable tax and reserve treatment now accorded to IBFs.[298] Nevertheless, offshore shell branches continue to be used widely by both U.S. and foreign banks.[299]

The Riegle-Neal Act and its implementing regulations prohibit an offshore shell branch that is "managed or controlled" by the U.S. office of a foreign bank from engaging in any type of activity in which a U.S. bank could not engage through its foreign branches or subsidiaries.[300] The standard for determining "managed or controlled" is whether a majority of the responsibility for business decisions or record-keeping rests with the U.S. office.[301] The Board has made clear that offshore shell branches are limited with respect to the *types* of activities in which they may engage but are not subject to the various quantitative or procedural

[296]As discussed above, the OCC and many states have modified asset pledge requirements to permit a foreign bank branch or agency to exclude IBFs from the liability base from which the asset pledge is computed. *See* § 1:03[2][e].

[297]Federal Reserve Board, Structure Data for U.S. Offices of Foreign Banks (as of September 30, 2011), available at http://www.federalreserve.gov.

[298]As noted, liabilities held in IBFs are excluded from the liability base in calculating asset pledge requirements. Also, reserve requirements are currently zero on nonpersonal time deposits and Eurocurrency liabilities, further reducing the need for an offshore shell branch. *See* 12 C.F.R. § 204.4(f).

[299]Until the early 1990s, foreign banks (like U.S. banks) controlled billions of dollars in assets and liabilities through offshore shell branches but were almost entirely unregulated in the U.S. even if their activities were managed through U.S. offices.

[300]12 U.S.C.A. § 3105(k)(1).

[301]12 C.F.R. § 211.24(g)(2). This is the same definition used in the Federal Financial Institutions Examinations Council (FFIEC) Form 002S, for the purpose of determining which U.S. branches and agencies of foreign banks manage or control offshore offices. *See* 61 Fed. Reg. 19, 524 to 526 (May 2, 1996) (Board commentary to final rule).

requirements imposed on the overseas activities of a U.S. bank.[302] Thus, foreign banks generally have more flexibility to conduct business through offshore shell branches than U.S. banks.

Offshore shell branches of foreign banks are generally not subject to direct supervision or examination by U.S. bank regulators.[303] Since 1992, however, foreign banks have been required to submit a supplement to the quarterly report of assets and liabilities (FFIEC 002) for each offshore shell branch that is managed or controlled by a U.S. office.[304] The reporting requirement was imposed in response to the perception of the Board and FFIEC that the prior "situation, in which foreign bank activities, including large and potentially volatile transactions with U.S. residents, escaped statistical reporting, needed to be addressed."[305]

Recent regulatory developments, such as the expanded advantages of IBFs and the elimination of reserves on Eurocurrency deposits, have diminished some of the original rationale for operating an offshore shell branch. Nevertheless, foreign banks continue to conduct a substantial volume of business through such branches.

[9] Financing Subsidiaries

Many foreign banks have established finance subsidiaries to issue commercial paper and other types of debt in the U.S. markets.[306] Finance subsidiaries typically allow foreign banks broader access to U.S. capital markets than the foreign bank could obtain directly due to frequent constraints on the authority of U.S. institutional investors to purchase the debt of foreign organizations.

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[302]*See* 61 Fed. Reg. 19,526 (final rule "excludes United States procedural or quantitative supervisory requirements that may apply to the offshore branch or subsidiary of a United States bank").

[303]In New York, however, the NYSBD has been given authority to examine records relating to offshore branches managed by New York branches of foreign banks. N.Y. Banking Law §§ 36(4), 200-c.

[304]57 Fed. Reg. 61,907 (Dec. 29, 1992).

[305]57 Fed. Reg. 61,907 (Dec. 29, 1992). Shortly before statistical reporting was required, a Federal Reserve Bank of New York study had estimated that the foreign bank share of the U.S. commercial lending market was approximately 30% if offshore assets and liabilities were included. *See* McCauley and Setha, Foreign Bank Credit to U.S. Corporations: The Implications of Offshore Loans, Fed. Res. Bank. N.Y.Q. Rev. 52 (Spring 1992). When the FFIEC 002 Supplement data were reported, the actual share turned out to be nearly 40%.

[306]Preamble to SEC Release No. IC-16093, 52 Fed. Reg. 42,280 (Nov. 4, 1987).

Typically, the foreign bank itself guarantees the obligations issued by its finance subsidiary, allowing the debt to be issued at a lower rate and reducing the bank's cost of funds. The proceeds generally can be used to fund both U.S. and overseas operations of the foreign bank. The funds are subject to U.S. reserve requirements only if they are advanced directly to a U.S. branch, agency, or bank subsidiary of the foreign bank.

[10] Export Trading Companies

The Bank Export Services Act[307] permits a BHC or a foreign bank, as well as other banking organizations, to establish an export trading company with consent of the Board.[308] An export trading company must be organized and operated principally for the purpose of exporting, or facilitating the export of, U.S. goods or services.[309]

An export trading company is permitted to engage only in activities related to international trade such as foreign exchange and financing services, consulting, international market research, transportation, warehousing, and advertising.[310] At least one-third of an export trading company's total revenue must be derived from the export of U.S. goods or services, and it must derive more revenue from the export of U.S. goods and services than from the importation of goods or services into the United States.[311]

As Congress envisioned it, the attractive feature of an export trading company was that it would give foreign and domestic bank holding companies the opportunity to participate in nonbanking, trade-related services such as importing and advertising.[312] To date, however, export trading companies have not been widely used by either domestic or foreign banks.

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[307] Tit. II of the Export Trading Company Act of 1982, Pub. L. No. 97-290, § 203, 96 Stat. 1233, 1236 to 1238 (codified at 12 U.S.C.A. § 1843(c)(14)).

[308] 12 U.S.C.A. § 1843(c)(14). An export trading company may be established upon general consent of the Board for certain well managed and well capitalized investors and through a 60-day notice procedure for other eligible investors. *See* 12 C.F.R. § 211.34.

[309] 12 C.F.R. § 221.32(a).

[310] 12 C.F.R. § 221.32(e).

[311] 12 C.F.R. § 221.32(e).

[312] *See* 48 Fed. Reg. 3,375, at 3,377 (Jan. 25, 1983) (Federal Reserve Board's proposed rule implementing ETC provisions of the BESA).

§ 1:4 Supervision and enforcement

[1] U.S. Bank Regulators' Focus on Compliance

The enactment of FBSEA in 1991 signaled a shift in focus of federal banking regulators to a more restrictive, penalty-based enforcement scheme than had previously been applied to foreign banks operating in the United States. While this approach was similar to the stepped-up enforcement actions taken against domestic banks in the wake of record bank failures in the 1980s, it nevertheless constituted a significant change for foreign banks. As a result, FBOs have had to devote substantially increased resources to their compliance efforts. In addition, the requirements of the USA PATRIOT Act impose further compliance burdens.

In this regard, the policy guidance and enforcement decisions of the federal banking agencies have consistently reflected the importance of maintaining internal compliance programs. For example, the *Interagency Policy Regarding Assessment of Civil Money Penalties* expressly takes into account the presence of an effective compliance program as a mitigating factor in assessing penalties for violation of laws and regulations.[313] In enforcement actions against the U.S. operations of foreign banks,[314] the Board has also repeatedly emphasized the importance of the involve-

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[Section 1:4]

[313] Board of Governors of the Federal Reserve System, *Interagency Policy Regarding Assessment of Civil Money Penalties*, June 3, 1998, reprinted in I F.R.R.S. 3-1605 (the presence or absence of a compliance program and its effectiveness is relevant in determining the appropriateness of initiating a civil money penalty assessment proceeding).

[314] *See, e.g.*, Fed. Res. Press Release (Oct. 7, 2010) (attaching a consent cease and desist order requiring HSBC North America Holdings to improve its enterprise-wide compliance risk management program); Fed. Res. Press Release (July 14, 2006) (attaching a written agreement requiring Banco Industrial de Venezuela, C.A. to improve its compliance program); Fed. Res. Press Release (Jan. 18, 1995) (attaching a written agreement with the PT Bank Ekspor Impor, Jakarta, Indonesia, and its New York agency requiring submission of a detailed plan primarily focused on improving the bank's compliance system and enhancing the bank's internal control procedures); Fed. Res. Press Release (Dec. 16, 1998) (PT Bank Ekspor Impor fined for violating its 1995 written agreement); Fed. Res. Press Release (Jan. 14, 1993) (attaching a written agreement with the PT Bank Niaga, Jakarta, Indonesia, and its Los Angeles agency office requiring submission of a written description of specific actions the board of directors of PT Bank Niaga proposes to take to improve its supervision over those responsible for the agency's overall performance, loan administration, and internal operations); Fed. Res. Press Release (Aug. 29, 1994) (attaching a written agreement with the Bangkok Metropolitan Bank, PLC, Bangkok, Thailand, and its San Francisco agency requiring the same written description required of PT Bank Niaga); Fed. Res. Press Release (Sept. 14, 1994) (attaching a written

ment of senior management of the U.S. operations and head office in the development and oversight of a compliance program. In response to these actions—and consistent with the requirements of IMLA, which expressly requires all financial institutions to adopt written anti-money laundering programs—foreign banks have made significant progress toward developing centralized compliance programs.

This part summarizes the requirements under each of the three principal elements of the supervisory regime applicable to foreign bank operations in the United States, i.e., reporting, examination, and enforcement requirements.

[2] Reporting Requirements

Like domestic banks, foreign banks operating in the U.S. are subject to a variety of federal and state reporting requirements, including those of the Board, the FFIEC, the SEC, the Department of Treasury's Financial Crimes Enforcement Network (FinCEN), and the Department of Commerce. The key federal reporting requirements are summarized in this section.[315]

[a] Forms FR Y-7 and FR Y-10

A FBO[316]—which is essentially any foreign organization that conducts U.S. banking operations—has numerous reporting obligations to the Board. Some reports are regular and periodic while others are event-driven. Of the periodic reports, perhaps the most significant is the Form FR Y-7 Annual Report of Foreign Banking Organizations, which includes the Nonbank Financial Information Summary. A related but event-driven report is the

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agreement with the National Bank of Greece and its branches in Boston and Chicago requiring the National Bank of Greece to submit a written plan to upgrade its supervision of the branches including the implementation of periodic onsite audits of the branches by head office personnel).

[315]Foreign banks that wish to establish a presence in a particular state should also evaluate potentially applicable state reporting requirements. *See* §§ 4:1 et seq.

[316]A foreign banking organization is defined by the Board to be any (1) foreign bank, or company that controls a foreign bank, that operates a U.S. branch, agency, Edge Act or Agreement Corporation, or commercial lending company organized in the United States; and (2) BHC organized outside the United States (which by definition means a foreign company that controls a U.S bank). *See* 12 C.F.R. § 211.21(n) (1999); General Instructions for Preparation of the Annual Report of Foreign Banking Organizations at 1.

Form FR Y-10 Report of Changes in Organizational Structure.[317]

The Form FR Y-7 (Annual Report of Foreign Banking Organizations) is the basic annual report that an FBO must submit to the Board within four months of the close of the FBO's fiscal year. The submission is generally available for public inspection, but the Board may grant confidential treatment upon request to parts of the report depending on the circumstances.

The FR Y-7 consists of financial information about the FBO's banking and nonbanking operations in the U.S. Among other things, it requires the submission of consolidated financial statements of bank subsidiaries, shares and shareholder information, risk-based capital ratios, and information concerning the ownership and structure of the FBO's operations. Form FR Y-7 also requires detailed information about the organization, management, and ownership of the FBO and its affiliates. Such ownership information may be relied upon by a U.S. branch or agency of a foreign bank, or other covered financial institutions, to satisfy the USA PATRIOT Act's requirements concerning record-keeping requirements for a correspondent account of a foreign bank.[318]

In December 2002, the Federal Reserve Board reorganized and simplified form FR Y-7. It created forms FR Y-7N and FR Y-7NS for reporting of financial data concerning nonbank subsidiaries, replacing the Nonbank Financial Information Summary that previously was required to be filed with the FR Y-7. The Federal Reserve Board also removed the risk-based capital information from the FR Y-7 to a form, FR Y-7Q.

Form FR Y-10 is an event-driven report that must be filed to account for significant changes in the U.S. operations of an FBO.[319] "Reportable transactions" include the initial commencement of banking or certain nonbanking operations (either directly or through subsidiaries), the commencement of a new activity, the termination of a previously reportable activity, acquisitions, changes to previously reported items, and openings and closings

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[317] 12 U.S.C.A. § 3105(c)(2); 12 C.F.R. § 225.5(b). All of the forms discussed in this section, as well as instructions for their completion, are available at http://www.federalreserve.gov.

[318] *See* 31 C.F.R. § 103.177(a)(2).

[319] In June 2007, the Federal Reserve combined Forms FR Y-10, FR Y-10f, FR Y-10S, and FR 2058 into Form FR Y-10. Form FR Y-10f replaced Form FR Y-7A, which was used to report structural information concerning a FBO's U.S. offices, bank subsidiaries, and nonbank subsidiaries directly or indirectly engaged in business in the United States. In April 2008, the Federal Reserve adopted a new schedule to FR Y-10 to collect data on domestic branches of depository institutions and Edge or Agreement Corporations.

or relocations of U.S. branches, agencies, and representative offices. Form FR Y-10 must be filed within 30 calendar days of any such reportable transaction.

[b] Form FR Y-8

Foreign banks with U.S. banking subsidiaries must file a Form FR Y-8, which collects information on transactions between an insured depository institution and its affiliates that are subject to the restrictions of Section 23A of the FRA.[320] The FR Y-8 requires information on the outstanding aggregate amounts of various types of "covered transactions" such as the purchase of equity or securities from, or the extension of credit to, affiliates. A separate report must be completed for each insured depository institution. The report must be submitted on a quarterly basis to the appropriate district Federal Reserve Bank for each reporting institution.

[c] Form FFIEC 002

The Form FFIEC 002 Report of Condition consists of balance sheet and off-balance-sheet information, including detailed supporting schedule items, from all U.S. branches and agencies of foreign banks. It must be filed quarterly with the appropriate Federal Reserve Bank.[321] The report is comparable to the quarterly reports of condition (or "Call reports") that must be filed by U.S.-chartered commercial banks and Edge Act Corporations.

[d] Form FFIEC 002s

A foreign bank that manages or controls a non-U.S. shell branch from a U.S. branch or agency must file a supplementary schedule, Form FFIEC 002s, on a quarterly basis with its FFIEC 002.[322] The report collects data on the offshore branch's assets and liabilities to ascertain its volume of banking business with U.S. residents. Institution-specific data collected by the Form FFIEC 002s are confidential though aggregate data are published occasionally in the Federal Register.

[e] Department of Commerce Reports

Foreign banks may occasionally be required to file reports to the U.S. Department of Commerce. Any foreign investor, includ-

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[320] 12 U.S.C.A. § 371c (Section 23A of the FRA); *see* 12 U.S.C.A. § 3105(c); 12 C.F.R. § 225.5(b) (reporting requirement for foreign banks). Previously, FBOs filed a slightly modified version of the form called Form FR Y-8f; now, they file the same form (FR Y-8) as domestic bank holding companies.

[321] 12 U.S.C.A. § 3105(c); 12 C.F.R. § 304.3(b).

[322] The definition of "manages or controls" is discussed in § 1:3[8].

ing a foreign bank, must submit Form BE-13 to report the acquisition, establishment, or purchase of assets of a U.S. business enterprise.[323] Thus, a foreign bank will need to submit a BE-13 report upon making its initial investment in a U.S. bank or nonbank subsidiary. The Department of Commerce also requires foreign investors, including foreign banks, to submit survey information concerning their U.S. operations once every five years on Form BE-12.[324]

[f] Suspicious Activity Reports

Each financial institution—including a subsidiary, branch, or agency of a foreign bank—must file a SAR with the Treasury Department's FinCEN if the institution knows of or suspects money laundering activity or certain other criminal violations. Specifically, a SAR must be filed for any known or suspected violation of federal law that involves: (1) insiders (including directors, officers, employees, agents, or other institution-affiliated parties) regardless of the amount of loss; (2) violations of criminal law aggregating $5,000 or more when a suspect can be identified; (3) violations of criminal law aggregating $25,000 or more regardless of whether a suspect can be identified; and (4) transactions of $5,000 or more in which money laundering or a violation of the BSA is known or expected.[325]

The SAR must be filed with FinCEN within 30 days after the initial detection of facts constituting the basis for the report.[326] Failure to file an SAR may subject the financial institution, its directors, officers, employees, agents, or other institution affiliated parties to supervisory action.[327] In certain circumstances, the BSA provides safe-harbor protection from liability that might otherwise result from reporting the suspicious activity.

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[323]The Department's authority to require reports concerning foreign direct investment in U.S. businesses is derived from the International Investment and Trade in Services Survey Act. *See* 12 U.S.C.A. §§ 3101 to 3108.

[324]58 Fed. Reg. 53,125 (Oct. 14, 1993).

[325]12 C.F.R. §§ 208.62; 21.24. A financial institution also must file an SAR whenever it knows of or suspects a violation of the U.S. criminal code relating to computer crimes. *See* Fed. Res. Board SR Letter 97-28 (ENF) (Nov. 6, 1997) (describing computer-related crimes subject to the SAR requirement). The Federal Reserve further has issued guidance clarifying with whom a SAR should be filed in the event that multiple agencies' regulations require submission of a SAR in a given scenario. *See* Fed. Res. Board SR Letter 10-8 (Apr. 27, 2010).

[326]12 C.F.R. §§ 208.62(d), 21.11(d).

[327]12 C.F.R. §§ 21.11(i), 208.62(i).

[g] Anti-Money Laundering Reporting Requirements

In the wake of the September 11 attacks and the USA PATRIOT Act, banking regulators have been examining the anti-money laundering compliance programs of both foreign and domestic banks with increased scrutiny. The BSA and its regulations require financial institutions to file a CTR with FinCEN for every currency or cash transaction exceeding $10,000, including withdrawals, deposits, currency exchanges, or other payments or transfers.[328] Multiple transactions on the same business day by or on behalf of the same person are treated as a single transaction for purposes of the CTR requirement.[329] To ease the compliance burden, the Treasury regulation allows institutions to maintain lists of designated "exempt persons" for whom CTRs are not required, including other U.S. depository institutions; certain federal, state, local, and quasi-governmental entities; companies listed on national stock exchanges and certain of their subsidiaries; and certain businesses and payroll customers with well-established transaction accounts.[330]

IMLA does not directly impose new reporting requirements, but it does require financial institutions, including foreign banks, to implement internal policies, procedures, and controls that include the reporting of known or suspected money laundering. For example, financial institutions must adopt due diligence programs for correspondent and private banking accounts that specifically address the circumstances for filing SARs.[331] IMLA also extends the requirement to maintain an anti-money laundering program much further than before so that all foreign bank operations in the U.S. (and indeed, many nonbanking organizations) now must comply.[332] This development too may result in a more frequent need for foreign banks to report suspected money laundering activity.

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[328] 31 C.F.R. § 1010.311.

[329] 31 C.F.R. § 1010.313(b). Likewise, all of the financial institution's branches are treated as one for purposes of the CTR requirement. 31 C.F.R. § 1010.313(a).

[330] 31 C.F.R. § 1020.315(a).

[331] *See* 31 C.F.R. § 1010.610 (mandatory due diligence program for correspondent accounts must include policies and procedures concerning when to file SARs); 31 C.F.R. § 1010.620 (due diligence program for private banking accounts must address reporting of suspicious activity "in accordance with applicable law and regulation").

[332] 31 U.S.C.A. § 5318(h); *see also* § 1:2. As discussed in § 1:2, a financial institution is deemed to be in compliance with the new requirement to maintain an anti-money laundering program if it is already complying with its federal regulator's existing regulations on the subject. 31 C.F.R. § 1020.210. *See also* 12

[3] Examination Requirements

Under FBSEA, the Board has central authority for the examination of all U.S. banking operations of foreign banks, including branches and agencies, bank subsidiaries, commercial lending companies, and all other affiliates that conduct a banking business in any state.[333] The Board is required, however, to coordinate examinations with the other federal and state supervisory authorities to avoid duplication and promote uniformity in the examination process.[334] In the years since FBSEA's enactment, the Board has worked with the Comptroller, the FDIC, and the NYSBD, as well as other state regulators, to implement a coordinated examination process.

In December 1998, the Board and the FDIC entered into a national agreement with state banking departments to coordinate state examination activities with those of the Board and FDIC. The Nationwide State/Federal Foreign Banking Organization Supervision and Examination Coordination Agreement (referred to as the "State/Federal Agreement") requires designation of a specific Federal Reserve Bank and FDIC Regional Office (if the foreign bank has an insured branch) as the responsible entities for all examination and supervisory purposes.[335] The agreement operates to provide FBOs with a single "regulatory point of contact" for the scheduling and planning of examinations. In addition, state bank supervisors have entered into the Nationwide Foreign Banking Organization Supervision and Examination Coordination Agreement (the "State Coordination Agreement"), which creates a structure for one state banking department to coordinate the examination and supervision of a FBO licensed in multiple states.[336]

[a] Risk-Focused Examination

U.S. branches and agencies of foreign banks are generally

C.F.R. § 21.21 (OCC regulations); 12 C.F.R. § 208.63 (Federal Reserve regulations); 12 C.F.R. § 326.8 (FDIC regulations).

[333] *See* 12 U.S.C.A. § 3105(c)(1)(A).

[334] 12 U.S.C.A. § 3105(c)(1)(B).

[335] A complete copy of the State/Federal Agreement is available at the Web site of the Conference of State Bank Supervisors (http://www.csbs.org/regulatory/Cooperative-Agreements/Documents/state_federal_fbo_agrmnt.pdf).

[336] The State Coordination Agreement is also available at www.csbs.org (http://www.csbs.org/regulatory/Cooperative-Agreements/Documents/state_fbo_agrmnt.pdf).

examined by federal banking regulators on a 12-month cycle.[337] The examination process includes three key components: (1) an evaluation under a rating system known as ROCA (Risk management, Operational Controls, Compliance, and Asset quality), calculated separately for each branch or agency and also on a combined basis for the entire FBO; (2) a consolidated evaluation of the foreign bank's U.S. bank and nonbank operations, known as the Summary of Condition; and (3) an evaluation of the support of the parent foreign bank, known as SOSA (Strength of Support Assessment).[338]

Implemented in 1995, the ROCA rating system reflected a shift in examination focus from asset quality to risk management.[339] It also placed a newfound emphasis on the maintenance of internal controls and compliance.[340] Under ROCA, a branch or agency is evaluated on the basis of three review components: risk management, operational controls, and compliance. For each, the branch or agency receives a score of 1 to 5. A score of 1 or 2 means that the branch is generally strong and no more than normal supervisory attention is warranted; a 3 represents a finding of supervisory concern warranting closer attention; and a 4 or 5 indicates serious weaknesses requiring urgent corrective action and potentially even a suspension or termination of operations.[341]

The first ROCA component, Risk Management, involves a de-

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[337]Some branches and agencies are eligible for an 18-month examination cycle if they meet requirements related to asset size and prior examination results. *See* 63 Fed. Reg. 46,118 (Aug. 28, 1998).

[338]An important source of information for foreign banks is the Board's Examination Manual for U.S. Branches and Agencies of Foreign Banks, which was prepared by a task force of representatives from the principal federal and state bank regulatory agencies with the goal of providing uniform guidance. *See Risk Management Anxiety Rises as Manual Nears*, 6 Thomson's Int'l Banking Reg., Aug. 22, 1994, at 4; William Acworth, *Regulators Still Battling Over New Exam Manual*, 6 Thomson's Int'l Banking Reg., Sept. 26, 1994, at 1. The manual explains the rating and examination system for foreign banks and provides guidance on risk management policies, external and internal audit programs, and other topics. It is available at http://www.federalreserve.gov. *See also* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations (Oct. 23, 2000).

[339]*See Asset Quality Fades as Priority; 'Commitment' Letters Prevalent*, 6 THOMSON'S INT'L BANKING REG., June 20, 1994, at 5. ROCA replaced the AIM (Asset quality, Internal controls and operations, and Management) rating system that had been used previously.

[340]*See Asset Quality Fades as Priority; 'Commitment' Letters Prevalent*, 6 THOMSON'S INT'L BANKING REG., June 20, 1994, at 5.

[341]*See* Examination Manual for U.S. Branches and Agencies of Foreign Banking Organizations, available at http://www.federalreserve.gov.

termination of whether the branch or agency has implemented adequate methods to control risk exposure resulting from its activities. Senior management of the foreign bank is expected to be involved in developing and approving the risk management system applicable to U.S. operations.[342]

The second ROCA component evaluates whether the branch or agency has in place sufficient Operational Controls to ensure the reliability of accounting and financial information. Among other things, this evaluation involves an assessment of the independence and effectiveness of auditing systems.[343]

The third ROCA component, Compliance, requires branches and agencies to demonstrate compliance with all applicable state and federal laws and regulations, including reporting requirements. To the extent possible, responsibility for compliance should be assigned to an officer who is independent from management and not involved in the internal auditing process.[344]

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[342] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 15–16 (Oct. 23, 2000). In rating risk management procedures, examiners will consider:

1. the branch or agency's ability to identify, measure, and control the risks inherent in its activities;
2. the soundness of the qualitative and quantitative assumptions implicit in the risk management system;
3. whether risk policies, guidelines, and limits are consistent with activities, management's experience, and the overall financial strength of the branch and foreign banking organization;
4. whether the management information systems are sufficient to accurately monitor risk exposure and compliance with established limits; and
5. management's ability to recognize and accommodate new risks and identify those not readily quantified in a risk management system.

[343] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 17–18 (Oct. 23, 2000). Examiners will specifically consider:

1. the adequacy of controls and level of adherence to existing procedures and systems;
2. the independence, frequency, scope, and adequacy of the branch or agency's internal and external audit function;
3. the severity of internal control and audit exceptions and whether exceptions are effectively tracked and timely resolved;
4. the adequacy and accuracy of management information reports; and
5. whether the system of controls is regularly reviewed to keep pace with changes in the branch's business plan and laws and regulations.

[344] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 19 (Oct. 23, 2000). Examiners will specifically review:

The final ROCA component, Asset Quality, involves an evaluation of overall asset quality though this aspect of the examination process has received less emphasis than under the previous examination rating system. Asset quality is evaluated to determine whether the institution has sufficient capital to absorb prospective losses "and, ultimately, whether it can maintain its viability as an ongoing entity."[345] If support from the FBO is questionable, the asset quality of the branch or agency will be carefully scrutinized to determine whether the branch or agency can meet its obligations on a stand-alone basis. If the FBO is in satisfactory condition, however, it is presumed to be able to support the branch, and the assessment of asset quality "would not in and of itself be a predominant factor in the branch's overall assessment."[346]

Finally, a branch or agency is assigned a composite rating reflecting its overall quality of operations.[347] The ROCA ratings of an institution are revised whenever there is strong evidence that the financial condition or risk profile of the institution has changed significantly. As with the examination ratings of domestic banks, ROCA ratings are confidential: they are disclosed only to the bank itself and other U.S. regulators.

In addition to a ROCA rating, foreign banks receive a consolidated examination report. This "Summary of Condition," which is prepared by the Federal Reserve, is an assessment of the U.S. business operations of a foreign bank as a whole, including nonbank operations. The Summary of Condition is based upon a Combined Rating for U.S. Operations, which, like ROCA, is on a

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1. the level of adherence to applicable state and federal laws and regulations and supervisory actions;
2. the effectiveness of written compliance procedures and training of line personnel;
3. management's ability to submit required regulatory reports in a timely and accurate manner;
4. management's ability to identify and correct compliance issues; and
5. whether the internal audit function checks for compliance with applicable state and federal laws and regulations.

[345] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 20 (Oct. 23, 2000).

[346] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 20 (Oct. 23, 2000).

[347] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 21 (Oct. 23, 2000).

scale of 1 to 5 with ratings of 1 and 2 warranting only normal supervisory attention.[348]

Finally, each FBO receives a strength-of-support assessment (SOSA) rating, which evaluates the support the FBO provides to its U.S. operations. Factors considered in the SOSA rating include the FBO's financial condition, the quality of its home-country supervision, its internal compliance and control procedures, and the riskiness of its non-U.S. activities. The SOSA rating is assigned by the Board in consultation with other appropriate agencies. The SOSA includes two components: an assessment of the FBO's ability to meet its U.S. obligations, and an evaluation of whether the FBO maintains adequate internal controls and compliance procedures at its U.S. offices (regardless of its financial condition). The first component results in a rating of "A" through "E" with A being the highest. The second component results in the placing of an asterisk next to the letter grade if control risks are apparent. SOSA ratings are for internal supervisory use only and are not disclosed even to the FBO itself. However, supervisory concerns that are discovered in the SOSA process will be communicated to the FBO's management and home-country supervisor if deemed appropriate.[349]

[b] Consequences of Examination Results

A foreign bank's ratings can profoundly affect its ability to make acquisitions and expand its business operations. In particular, a strong Summary of Condition report and high ROCA ratings can result in expedited Board approval for acquisitions and new activities.[350] Conversely, poor performance can thwart a foreign bank's efforts to acquire or establish new offices or to engage in expanded banking or nonbanking activities. Many foreign banks have found that the Board will not process applications for expansion from a foreign bank that has a branch, agency, or nonbanking affiliate with a "3" or lower rating.[351]

At a minimum, low ratings will result in increased supervisory

[348] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 11 (Oct. 23, 2000).

[349] *See* Fed. Res. SR 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations, 4 (Oct. 23, 2000).

[350] *See* 12 C.F.R. §§ 225.13, 225.23; Fed. Res. Board, SR Letter 97-13 (APP) (Apr. 24, 1997) (discussing the Summary of Condition and ROCA ratings a FBO must have in order to take advantage of the expedited approval process).

[351] Foreign banks seeking to expand their U.S. operations must also be careful to maintain a strong record of compliance with consumer laws, to the extent

attention from federal bank regulators. Such increased attention could take the form of more frequent examinations of problem areas, the imposition of special audit procedures, and informal enforcement actions. Consequently, since the enactment of FBSEA, foreign banks have been forced to devote considerable attention to their performance on federal examinations.

[c] Special Supervisory Considerations for Large Complex Foreign Banking Organizations

Foreign and domestic banking organizations that qualify as large complex banking organizations (LCBOs) are subject to additional supervisory scrutiny. A banking organization qualifies as an LCBO if it meets certain criteria relating to the size of its on- and off-balance sheet risk exposures, the breadth of its range of products and services, the complexity of its supervision in the U.S. and abroad, and the extent of its participation in large-value payment and settlement systems.[352] LCBOs must undergo continuous monitoring and assessment of their risk profiles by teams of supervisors sent by the Board. They are also subject to frequent—at least quarterly—reassessments of their supervisory plans and programs.[353] The Board prepares a comprehensive annual report on the condition of each LCBO.

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they are applicable. Even U.S. offices of foreign banks that are not required to comply with the CRA have voluntarily developed community lending programs in an effort to build goodwill and create a favorable record in support of potential applications. *See New CRA Rules May Give Foreign Banks More Options*, 6 THOMSON'S INT'L BANKING REG., Oct. 17, 1994, at 1; *UBS Readies Plans for CRA Subsidiary*, 6 THOMSON'S INT'L BANKING REG., May 23, 1994, at 1. In addition to the CRA, the U.S. operations of foreign banks are potentially subject to a number of other consumer laws, including: Regulation B, Equal Credit Opportunity (12 C.F.R. § 202), Regulation C, Home Mortgage Disclosure (12 C.F.R. § 203), Regulation E, Electronic Fund Transfers (12 C.F.R. § 205), Regulation Z, Truth in Lending (12 C.F.R. § 226). Regulation CC, Availability of Funds and Collection of Checks (12 C.F.R. § 229), Regulation DD, Truth in Savings (12 C.F.R. § 230), and the Fair Credit Reporting Act (15 U.S.C.A. § 1681).

[352] *See* Fed. Res. Board, SR Letter 98-13 (SUP.IB) (June 3, 1998) (applying elements of the supervision framework to qualifying FBOs); Fed. Res. Board, SR Letter 97-24 (SUP), Risk-Focused Framework for Supervision of Large Complex Institutions (Oct. 27, 1997) (describing Board's risk-focused framework for complex institutions with assets in excess of $1 billion).

[353] *See* Fed. Res. Board, SR Letter 99-15 (SUP), Risk-Focused Supervision of Large Complex Banking Organizations (June 23, 1999) (clarifying and providing specific guidance on applicability of program to LCBOs).

[4] Enforcement

[a] The Enforcement Process

As discussed in Section 1:2[3], foreign banks have been subject to more intensive regulatory scrutiny since the enactment of FBSEA. The enhanced supervision has resulted in an increase in the frequency of enforcement actions by federal banking agencies against foreign banks. Generally, foreign banks are subject to federal enforcement action only on the basis of their U.S operations though a federal banking agency may take action on the basis of extraterritorial factors such as the adequacy of the foreign bank's home-country supervision. This section discusses the most common enforcement issues affecting foreign banks.

[i] Informal Enforcement Actions

Informal enforcement actions usually result in nonpublic agreements between banks and regulators to address specific areas of regulatory concern. Typically, the bank commits to undertake a specific course of action to correct the weaknesses identified by banking regulators in order to avoid a formal enforcement action that would be public and could result in more stringent measures. The most frequently used informal enforcement tools are commitment letters and memoranda of understanding. A commitment letter details the corrective action that the bank plans to take to address the regulators' concerns.[354] A memorandum of understanding, in contrast, is an agreement between the regulatory agency with bank officers and sets forth each party's understanding of the actions that the bank must take to address deficiencies or criticisms.[355] Another mechanism by which regulators sometimes express concerns and suggest corrective action is the transmittal letter for an examination report. It is advisable for banks to respond promptly with an acknowledgment of the concern and a plan for corrective action because failure to heed such a warning can be a factor in the assessment of civil money

[354] Although commitment letters are generally not made public, federal banking agencies occasionally publish statistics about the frequency of their use. In 2008, for example, the OCC issued nine commitment letters against banks. *See* Testimony of Comptroller of the Currency John Dugan Before the Financial Services Committee of the House of Representatives, 7 (Mar. 20, 2009).

[355] In 2008, the OCC issued 17 memoranda of understanding. *See* Testimony of Comptroller of the Currency John Dugan Before the Financial Services Committee of the House of Representatives, 7 (Mar. 20, 2009).

penalties.[356]

[ii] Formal Enforcement Actions

The key features of formal enforcement actions are that they are made public[357] and are more readily enforceable than informal actions. Accordingly, institutions seek to resolve regulatory issues through informal enforcement whenever possible.

The two principal types of formal enforcement actions are: (1) written agreements, which are administratively enforceable; and (2) cease and desist orders, which are administratively and judicially enforceable.[358] In a written agreement, the institution consents to a specific remedial plan to correct the weaknesses or regulatory concerns at issue.[359] The bank's failure to adhere to the written agreement can result in the imposition of a cease and desist order and civil money penalties.[360]

The appropriate banking agency may issue a cease and desist order for: (1) an unsafe or unsound banking practice; (2) violation of a law, rule, or regulation; (3) violation of any condition imposed by the agency in connection with the granting of any application; or (4) a violation of a formal written agreement.[361] The agency must provide the bank with notice of the alleged violation and, if the bank does not consent to the issuance of the order, a hearing before issuing the cease and desist order.[362] The order may require the bank to stop the allegedly unlawful practice and also to take affirmative action to correct the conditions resulting from the practice.[363] If the alleged violation unjustly enriched the institution or involved a reckless disregard for the law, the agency may

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[356] *See* Board of Governors of the Federal Reserve System, *Interagency Policy Regarding Assessment of Civil Money Penalties*, June 3, 1998, reprinted in I F.R.R.S. 3-1605.

[357] *See* 12 U.S.C.A. § 1818(u).

[358] Formal enforcement may also include the assessment of civil money penalties and, potentially, the termination of a foreign bank's branch, agency, or subsidiary. These penalties are discussed below.

[359] Formal written agreements are authorized by 12 C.F.R. § 265.11(a)(15), which specifies that each Federal Reserve Bank has authority to enter into written agreements with institutions subject to the Board's supervisory jurisdiction after obtaining approval from the Director of the Division of Banking Supervision and Regulation and the Board's General Counsel.

[360] 12 U.S.C.A. § 1818(b)(1)(i)(2)(A).

[361] 12 U.S.C.A. § 1818(b)(1). The IBA makes applicable to foreign banks, branches, and agencies the enforcement provisions of Section 8 of the FDI Act, 12 U.S.C.A. § 1818. *See* 12 U.S.C.A. § 3108(b)(1).

[362] 12 U.S.C.A. § 1818(b)(1).

[363] 12 U.S.C.A. § 1818(b)(1).

order the bank to make restitution or provide reimbursement, indemnification, or guaranty against loss.[364]

[iii] Civil Money Penalties

Civil money penalties may be assessed by the appropriate federal banking agency according to a three-tiered structure: (1) up to $5,000 a day for the violation of any law or regulation, final or temporary cease and desist order, written agreement, or written condition in connection with the grant of an application; (2) up to $25,000 a day if the violation was part of a pattern or practice of misconduct or caused more than a minimal loss or if the institution recklessly engaged in an unsafe or unsound practice; and (3) up to $1 million a day or one percent of the total assets of the institution (whichever is less) for knowingly committing such a violation or knowingly engaging in an unsafe or unsound practice.[365]

Penalties may be assessed and collected upon written notice from the appropriate agency though the institution may obtain a hearing if requested within 20 days.[366] In determining the amount of a civil money penalty, the agency is required to consider as potential mitigating factors the size and financial resources of the institution, the good faith of the institution, the gravity of the violation, the history of previous violations, and "such other matters as justice may require."[367]

FBSEA amended the IBA to add violations of the IBA as a specific basis for imposing civil money penalties on a foreign bank or any of its offices or subsidiaries. Such a violation of the IBA or its regulations will result in a civil penalty of up to $25,000 per day.[368] The penalty is to be assessed by the Board or the OCC under the same procedure as described above, including manda-

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[364] 12 U.S.C.A. § 1818(b)(6); *see* Fed. Res. Press Release (Mar. 28, 1997) (ordering The International Commercial Bank of China to make restitution for its profit of $17.3 million for acquiring control of the Chinese American Bank without filing a complete application).

[365] 12 U.S.C.A. § 1818(i)(2); 12 C.F.R. § 263.65(b)(2) (adjusting for inflation the maximum civil money penalties to $7,500 for a Tier 1 penalty, $37,500 for a Tier 2 penalty, and $1,375,000 for a Tier 3 penalty). The Board has separate authority to assess civil penalties for certain violations of the BHC Act and the FRA. *See* 12 U.S.C.A. § 1847 (authorizing Board to assess civil money penalties for violations of the BHC Act); 12 C.F.R. § 204.7(a) (authorizing Federal Reserve Banks to assess money penalties for failure to maintain required reserves).

[366] 12 U.S.C.A. § 1818(b)(i)(2)(E).

[367] 12 U.S.C.A. § 1818(i)(2)(G).

[368] 12 U.S.C.A. § 3110(a)(1); 12 C.F.R. § 263.65(b)(5) (adjusting for inflation the maximum penalty from $25,000 to $37,500).

tory consideration of the same mitigating factors.[369]

[iv] Termination

Section 202 of FBSEA allows the Board to terminate a foreign bank's state-licensed branch, agency, or commercial lending subsidiary under certain extraordinary circumstances. Termination is authorized where: (1) the foreign bank is not subject to consolidated comprehensive supervision (CCS) in its home country and the home-country supervisor is not making demonstrable progress toward establishing arrangements for CCS;[370] or (2) there is reasonable cause to believe that the foreign bank or any of its affiliates has committed a violation of law or engaged in an unsafe or unsound banking practice in the United States, and as a result, continued operation would be inconsistent with the public interest or statutory standards.[371]

In deciding whether to order termination, the Board may take into account the needs of the community, the length of operation of the foreign bank, and its relative size in its home country.[372] The Board is required to consult with the relevant state banking supervisor and to provide the bank with notice and an opportunity for a hearing unless expedited termination is necessary to "protect the public interest."[373]

With respect to federally licensed branches and agencies, the

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[369] 12 U.S.C.A. § 3110(a)(2).

[370] Following a determination that a foreign bank does not meet the CCS standard, the Board will consider 16 criteria to determine whether to terminate the foreign bank's U.S. operations or impose supervisory constraints on the Bank. *See* 12 C.F.R. § 211.30(b). These criteria include, among others, whether the bank's home-country supervisor is "actively working" toward CCS and is making demonstrable progress; whether the bank has effective internal control systems; the soundness of the bank's overall financial condition; the proportion of the bank's total assets and liabilities that are booked in its home country, and any other information relevant to the safety and soundness of the U.S. operations of the foreign bank.

[371] 12 U.S.C.A. § 3105(e)(1)(B); *see* Fed. Res., NYSBD and FDIC Press Release (Nov. 2, 1995) (ordering The Daiwa Bank, Limited to terminate its U.S. operations for unauthorized securities trading, misappropriation of customers' funds, and submitting false reports to bank examiners). The Board is also authorized to terminate representative offices of foreign banks. 12 U.S.C.A. § 3107(b); 12 C.F.R. § 211.25(a).

[372] 12 U.S.C.A. § 3105(e)(1).

[373] 12 C.F.R. § 211.25(c) and (d).

Comptroller, rather than the Board, has termination authority.[374] However, if the Board has reasonable cause to believe that a foreign bank or any of its affiliates has engaged in conduct that would warrant termination of a state-licensed office, it may recommend termination of a federal branch or agency to the Comptroller.[375]

[b] Focus of Enforcement Actions

U.S. enforcement efforts with respect to foreign banks have tended to focus primarily on compliance with the BSA, including its anti-money laundering provisions and on the adequacy of foreign banks' internal controls. In the aftermath of September 11 and the USA PATRIOT Act, that focus has expanded to include enforcement of the obligations of foreign and domestic banks with respect to international money laundering. The Treasury Department's regulations implementing the IMLA establish the framework on which such enforcement activity will be based.

[i] The Bank Secrecy Act

IMLA expands the BSA's substantive anti-money laundering requirements but does not significantly change its enforcement framework. Compliance with the BSA is monitored by both the Treasury Department and the appropriate federal banking agencies. Treasury enforces the BSA's record-keeping and reporting requirements and assesses civil money penalties against financial institutions found to have violated the requirements.[376] Willful violations are subject to civil money penalties of the greater of the amount of the transaction that was not reported (up to $100,000) or $25,000 per violation.[377] Negligent violations are subject to a penalty of $500 per violation.[378]

The Board and the other federal bank regulatory agencies also have enforcement authority under the BSA. For instance, the federal banking agencies can issue cease and desist orders and assess money penalties on banks under their respective jurisdictions that fail to maintain adequate internal controls for BSA

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[374] 12 U.S.C.A. § 3102(i). In addition, the deposit insurance of an insured branch can be terminated by the FDIC under certain circumstances. 12 U.S.C.A. § 1818(a)(2).

[375] 12 U.S.C.A. §§ 3105(e)(5), 3102(i).

[376] 31 U.S.C.A. § 5321(a); 31 C.F.R. § 1010.810(a) and (f).

[377] 31 U.S.C.A. § 5321(a)(1); 31 C.F.R. § 1010.820(g).

[378] 31 U.S.C.A. § 5321(a)(6)(B); 31 C.F.R. § 1010.820(h).

compliance.[379] Such violations have been addressed through both written agreements and consent orders.[380] Frequently, the parties enter into a joint resolution that includes the NYSBD or other state authority, if applicable, as well as the Board and the institution. Such a resolution typically requires affirmative steps by the foreign bank to develop policies and procedures regarding internal controls. In many cases, the Board has required the development of internal controls governing all aspects of the operations of the U.S. office;[381] in addition, the Board sometimes will impose requirements for specific areas of concern such as asset quality or compliance with the BSA.[382]

For criminal money laundering offenses, federal bank regula-

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[379] *See, e.g.*, Fed. Res. Press Release (Oct. 7, 2010) (issuing a cease and desist order against HSBC North America Holdings for deficiencies in the consolidated entity's anti-money laundering controls); Fed. Res. Press Release (Nov. 13, 2008) (issuing a cease and desist order against Dresdner Bank AG for inadequate anti-money laundering controls); Fed. Res. Press Release (Dec. 19, 2005) (issuing a cease and desist order and civil money penalties of $80 million against ABN AMRO Bank N.V. for, among other violations, failure to maintain adequate controls to ensure compliance with U.S. anti-money laundering laws and regulations); Fed. Res. Press Release (Nov. 14, 2001) (issuing a cease and desist order and civil money penalties of $7.5 million against State Bank of India for, among other violations, failure to maintain adequate BSA internal controls at its three New York branches and its Chicago branch).

[380] *See, e.g.*, Fed. Res. Press Release (Dec. 1, 2000) (attaching written agreement in which Caisse Nationale de Credit Agricole consented to a detailed corrective action plan to improve internal control and risk management with respect to its New York state-licensed branch); Fed. Res. Press Release (May 18, 2000) (attaching written agreement in which Korean Exchange Bank agreed to a similar plan with respect to its California-licensed agency and three state-licensed branches).

[381] *See, e.g.*, Fed. Res. Press Release (Oct. 7, 2010) (HSBC North America Holdings, BHC of HSBC N.A.); Fed. Res. Press Release (May 16, 2002) (Maryland-licensed subsidiary bank of Allied Irish Banks); Fed. Res. Press Release (June 23, 2000) (various United States offices of Banco Bilbao Vizcaya Argentaria); Fed. Res. Press Release (Sept. 17, 1997) (New York branch and Article XII corporation of Skandinaviska Enskilda Banken); Fed. Res. Press Release (Oct. 26, 1993) (Florida agency office of Banco Boliviano Americana, S.A.); Fed. Res. Press Release (Jan. 14, 1993) (California agency office of PT Bank Niaga); Fed. Res. Press Release (July 7, 1992) (California branch of Habib Bank AG); Fed. Res. Press Release (Mar. 24, 1992) (California and New York agency offices and Pennsylvania branch office Bank of Seoul); Fed. Res. Press Release (Apr. 30, 1991) (New York branch and California agency of Bank Burmiputira Malaysia Berhad); Fed. Res. Press Release (Mar. 11, 1991) (New York branch and Georgia agency of Banca Nazionale Del Lavoro); Fed. Res. Press Release (Feb. 21, 1990) (California agency of Bank Dagang Negara).

[382] *See, e.g.*, Fed. Res. Press Release (Nov. 13, 2008) (suspicious activity reporting and customer due diligence; Dresdner Bank AG); Fed Res. Press Release (Jan. 18, 1995) (asset quality and compliance procedures; New York

tors are required to exercise their so-called "death penalty" enforcement authority under the BSA. Under that authority, a financial institution that has been convicted of a criminal money laundering violation faces automatic proceedings to terminate its operations and deposit insurance (if applicable). Upon receiving notice of the conviction, the FDIC is required to commence proceedings to terminate deposit insurance; the OCC must commence proceedings to revoke the license of a federally licensed branch or agency; and the Board must commence proceedings to terminate the license of the state-licensed branch or agency.[383] In addition, the appropriate federal banking agency has authority to remove or suspend an insured depository institution's directors, officers, or other institution-affiliated parties (IAPs)[384] for violations of the BSA or other law or regulation.[385]

[ii] Reporting Violations

Another area of enforcement activity against foreign banks has involved the failure to file timely and accurate reports. FBSEA provides substantial penalties for a foreign bank's submission of late, misleading, or inaccurate reports to federal banking agencies.[386] Penalties are assessed according to a three-tiered structure similar to that described above with penalties of $2,000; $20,000; or $1 million per day (or one percent of total assets of the foreign bank, whichever is less), depending on the severity of the offense.[387] Foreign banks can mitigate potential damages by maintaining procedures to avoid inadvertent error.

The Board has established a monitoring program in which the Federal Reserve Banks maintain a list of institutions that file

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agency of PT Bank Ekspor Impor Indonesia); Fed. Res. Press Release (Oct. 1, 1993) (Bank Secrecy Act; California branch of United Mizrahi Bank, Ltd.); Fed. Res. Press Release (Dec. 26, 1991) (Ljubljanska Banka, d.d., country exposure and credit concentration); Fed. Res. Press Release (Dec. 24, 1991) (asset quality; subsidiary banks of The Governor and Company of the Bank of Ireland).

[383] 12 U.S.C.A. §§ 93(d), 1818(w), 3105(i).

[384] 12 U.S.C.A. § 1818(e)(2)(A)(i). "Institution-affiliated parties" include directors, officers, employees, and controlling stockholders; certain stockholders who participate in the conduct of an insured depository institution's affairs; and certain independent contractors. 12 U.S.C.A. § 1813(u).

[385] 12 U.S.C.A. § 1818(e) and (g).

[386] 12 U.S.C.A. § 3110(c).

[387] 12 U.S.C.A. § 3110(c); 12 C.F.R. § 263.65(b)(6) (adjusting for inflation the maximum civil money penalties to $2,200 for a Tier 1 penalty, $32,000 for a Tier 2 penalty, and $1,375,000 for a Tier 3 penalty).

late reports.[388] Board staff evaluates this information on an ongoing basis to ensure that chronic late reporters are subjected to appropriate enforcement action.[389] The Board also monitors reports for accuracy and completeness and has imposed substantial penalties against foreign banks for allegedly filing inaccurate, incomplete, or misleading reports.[390] The Federal Reserve Banks assist the Board by identifying false reports in connection with their monitoring of late reporters.

[iii] Anti-Money Laundering

Several foreign banks have been the subject of federal enforcement actions for failing to take adequate measures to prevent and detect money laundering. In 2000, an undercover law-enforcement action designated "Operation Casablanca" resulted in the criminal money laundering convictions of two FBOs with U.S. operations—Bancomer, S.A., and Banca Serfin, S.A., both of MexiCo. Although the Board ultimately determined not to terminate the U.S. operations of Bancomer, S.A., it issued a consent cease and desist order requiring detailed enhancements of the bank's anti-money laundering programs and policies.[391] The Board simultaneously issued a written agreement with a

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[388] Fed. Res. Board, SR Letter 92-38 (FIS) (Oct. 15, 1992) and SR Letter 93-47 (FIS) (Aug. 13, 1993).

[389] The Board has not hesitated to assess substantial civil money penalties against foreign bank operations that fail to meet their reporting obligations. *See, e.g.*, Fed. Res. Press Release (Mar. 10, 2004) (attaching Order of Assessment of a Civil Money Penalty against Credit Agricole SA for the bank's failure to submit reports to the NYSBD); Fed. Res. Press Release (Mar. 25, 1998) (attaching Order of Assessment of a Civil Money Penalty against Habib Bank AG, Zurich, Switzerland, for the bank's incomplete and inaccurate FR Y-7 report), Fed. Res. Press Release (Nov. 29, 1994) (attaching: (1) Order of Assessment of a Civil Money Penalty against Bank Saderat Iran, Tehran, and its New York agency in the amount of $125,000 in connection with the bank's filing of late and incomplete regulatory reports and the agency's filing of false and misleading regulatory reports; (2) Order of Assessment of a Civil Money Penalty against Bank Melli Iran, Tehran, in the amount of $60,000 in connection with the bank's filing of late and incomplete regulatory reports; and (3) Order of Assessment of a Civil Money Penalty against Bank Sepah Iran, Tehran, in the amount of $100,000 in connection with the bank's filing of late and incomplete regulatory reports).

[390] *See, e.g.*, Fed. Res. Press Release (Sept. 17, 1997) (assessing a $2.5 million penalty against Skandinaviska Enskilda Banken for, among other things, filing allegedly inaccurate reports); Fed. Res. Press Release (July 11, 1997) (assessing a $900,000 penalty against Postipankki Ltd. for, among other things, filing allegedly false and misleading reports).

[391] *See* Fed. Res. Press Release (Dec. 12, 2000). No further enforcement action was necessary against Banca Serfin, S.A., because it had already ceased all U.S. operations.

Venezuelan bank requiring similar affirmative action to prevent money laundering. The Board has imposed similar requirements in other enforcement actions directed at foreign banks.[392]

As discussed in Section 1:2, the IMLA and its implementing regulations strengthen the existing anti-money laundering requirements applicable to financial institutions, including the U.S. operations of foreign banks. Since the enactment of IMLA and the promulgation of its implementing regulations, the rapid pace of BSA/AML-related enforcement actions against U.S. offices of foreign banks has continued if not accelerated.[393]

§ 1:5 Conclusion

Foreign banks have taken advantage of the equal access that they have been afforded to participate in the United States banking market. Although their market share relative to U.S. banks has declined somewhat in recent years, foreign banks remain sizable participants in U.S. wholesale banking markets and, through subsidiaries, in retail banking markets as well. Foreign banks have played a critical role in meeting the credit needs of the U.S. economy, facilitating international trade with the U.S., and fostering competition and innovation in the U.S. banking markets.

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[392] *See, e.g.*, Fed. Res. Press Release (Oct. 7, 2010) (issuing a cease and desist order against HSBC North America Holdings for deficiencies in the consolidated entity's anti-money laundering controls); Fed. Res. Press Release (June 23, 2000) (attaching written agreement in which Banco Bilbao Vizcaya Argentaria, S.A., agreed to implement enhanced anti-money laundering policies and procedures); Fed. Res. Press Release (May 18, 1998) (announcing entry of temporary cease and desist orders against five FBOs operating in the U.S. to address "serious deficiencies in their anti-money laundering programs").

[393] *See, e.g.*, Fed. Res. Press Release (Oct. 7, 2010) (issuing a cease and desist order against HSBC North America Holdings for deficiencies in the consolidated entity's anti-money laundering controls); Joint Press Release of Financial Crimes Enforcement Network and Office of the Comptroller of the Currency (Apr. 28, 2008) (attaching consent order against New York branch of United Bank for Africa, PLC, which included a $15 million civil money penalty); Joint Press Release of Federal Reserve Board, Financial Crimes Enforcement Network, Office of Foreign Assets Control, NYSBD, and Illinois Department of Financial and Professional Regulation (Dec. 19, 2005) (attaching cease and desist order against New York and Chicago branches of ABN Amro Bank N.V., which included $80 million civil money penalty); OCC News Release (Feb. 25, 2005) (attaching consent order against New York branch of Arab Bank PLC, which included contraction of the branch's activities and conversion to an agency); OCC News Release (Feb. 2, 2005) (attaching cease and desist order against New York branch of Banco de Chile); Federal Reserve News Release (Feb. 2, 2005) (attaching cease and desist order against Miami branch of Banco de Chile).

At the same time, foreign banks have encountered significantly increased regulation from the federal government. Much of the enhanced scrutiny has resulted from legislation specifically aimed at foreign banks such as the IBA and FBSEA. Other changes have been the result of more generally applicable requirements such as those imposed by the USA PATRIOT Act and the Dodd-Frank Act. In addition, foreign banks have gradually become subject to tougher, more penalty-focused enforcement efforts by federal regulators. The overall trend toward more extensive federal regulation continued with passage of the Dodd-Frank Act, and is unlikely to abate, considering the prominence of such issues as antiterrorism and corporate misconduct and the U.S. economy's recovery from the financial crisis of 2008.

Nevertheless, the current outlook for the U.S. operations of foreign banks remains favorable. As a result of two important laws modernizing the U.S. banking market—namely, the Riegle-Neal Act and the GLB Act: foreign banks now have the opportunity to participate in interstate banking and nonbanking financial activities much more freely than in the past. A regulatory framework is in place to allow foreign banks and domestic banks to pursue new business opportunities with much greater flexibility, and the legal foundation exists for foreign banks to increase both their banking and nonbanking activities in the United States. Most recently, the Dodd-Frank Act made sweeping changes to the financial regulatory landscape for both domestic and foreign banks. The ultimate impact of these changes remains uncertain given the number of regulations that are required to implement the Act but have not yet been promulgated.

Appendix 1A
U.S. Banking Operations of Foreign Banks: Regulation by Federal and State Banking Authorities

State Banking Department

Primary Federal Regulator

Additional Role for Federal Reserve

- **Commercial Bank Subsidiaries**
  - National Bank
    No
    OCC
    Yes
  - State Member Bank
    Yes
    Fed
    N/A
  - State Nonmember Bank
    Yes
    FDIC
    Yes
- **Branches & Agencies**
  - State Branches
    Yes
    Fed
    N/A
  - Federal Branches
    No
    OCC
    Yes
  - Commercial Lending Companies
    Yes
    Fed
    N/A
  - Edge Corporations

No
Fed
N/A

- Agreement Corporations
  Yes
  Fed
  N/A
- Representative Offices
  Yes
  Fed
  N/A