International Lawyer

Volume 15 | Number 4 | Article 13

1981

Caribbean Banking Subsidiaries and the International Banking Act of 1978

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Introduction

For years, businesses from the United States and the other industrialized nations have relied, to their advantage, upon the domestic tax treatment and tax treaty structures prevalent in the Caribbean tax havens in planning their U.S. and foreign operations. In addition to the use of tax haven jurisdictions by commercial entities (frequently by the formation of financing subsidiaries), American banks have increasingly used the "offshore" branch as a method of obtaining material tax benefits in conducting transactions in the Euro-currency markets. The use of offshore subsidiaries organized in the tax haven jurisdictions by major banks is a less well-known, but beneficial, practice. The use of the offshore banking subsidiary as a vehicle for major financial institutions from abroad to enter the United States market is potentially appealing. The impact of the International Banking Act of 1978 (the "Act")[1] simplifies and unifies the procedures to be observed in the commencement of U.S. banking operations by Caribbean subsidiaries of major foreign banks. While the Act facilitates the organization of branches of foreign banks in the United States, it also highlights certain philosophical conflicts among bank regulators. The conflicts arise not because of a divergence of the goals of the United States' regulators from those of their foreign counterparts, but in the methods to be used in achieving the common goal. Both United States and foreign bank regulators seek to ensure the development of a sound international banking system. Foreign regulators frequently feel that the attitude of the United States' authorities in their extraterritorial application of United States' laws is chauvinistic and improper. This article will review the recent development of foreign banking activity in the United States, the regulatory philosophies and proce-

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[1]International Banking Act of 1978, PUB. L. No. 95-369, 92 Stat. 607 (codified in scattered sections of 12 U.S.C. (Supp. II 1978) [hereinafter cited as the IBA]).

dures affecting offshore banks in the Caribbean and the impact of the Act on the formation and operation of foreign branches in the United States.

I. The Recent Development of Foreign Banking in the United States

The establishment of foreign banking facilities in the United States in significant numbers is a relatively recent development. Little foreign interest in American banking opportunities was excited, or tolerated, during the isolationist periods of American history prior to World War II. As the influence of American commerce and the dollar as a world currency expanded during the post-War period, so did foreign interest in American banking activities. During the initial developmental period following the War, expansion of American banks into foreign jurisdictions and foreign banks into the United States were equally inhibited by considerations of reciprocity.[2] The reciprocity factor was, and remains, a major feature of state legislative and regulatory policy which serves to inhibit development of foreign banking in this country.

New York, California, and Illinois, recognizing the substantial benefit to financial institutions based in those jurisdictions, were among the first to permit the establishment of foreign banking operations in their territories. Thus, in 1959, New York enacted legislation permitting deposit-taking foreign branches;[3] California, in 1964, authorized the taking of deposits by foreign branches but only if the foreign bank was approved for Federal Deposit Insurance Corporation (FDIC) insurance which was not available prior to the adoption of the Act.[4] Illinois followed suit in 1973.[5] Prior to the adoption of the Act, there was no federal legislation pursuant to which a foreign bank could, independently, carry on its activities in the United States other than by forming, as a subsidiary, a national bank. By the time the Act was adopted, however, ten states clearly permitted foreign banking institutions to carry on activities in their respective jurisdictions,[6] and a good argument can be made that an eleventh state also permitted foreign banking activity.[7] Thirty states and the District of Columbia had no legis-

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[2]*See, e.g.*, Glidden and Shockey, *U.S. Branches and Agencies of Foreign Banks: A Comparison of the Federal and State Chartering Options*, 1980 U. ILL. L. F. 65, 75-76 (1980) and authorities cited therein.

[3]N.Y. Banking Law § 202-a (McKinney 1971).

[4]CAL. FIN. CODE § 1756.1 (Deering 1978); IBA § 6, 12 U.S.C. § 3104 (Supp. II 1978).

[5]ILL. REV. STAT. Ch. 16-1/2, §§ 501 *et seq.* (1978).

[6]*See* ALAS. STAT. §§ 06.05.360, .367, .10.010 to .050 (1978); CAL. FIN. CODE §§ 1750-1758 and 3500-3543 (Deering 1978); FLA. STAT. ANN. § 659.67 (West 1979); GA. CODE ANN. §§ 41A-3301-3312 (1978); HAW. REV. STAT. §§ 403-5, -16 (1976); ILL. REV. STAT. ch. 16-1/2 §§ 501-519 (1978); MASS. GEN. LAWS ANN. ch. 167, §§ 37-45A (1971); N.Y. Banking Law §§ 200-209 (McKinney 1971); OR. REV. STAT. §§ 706.005, 713.010-.110 (1975); WASH. REV. CODE §§ 30.04.290-.300, 30.42.010 to .900 (1977).

[7]*See* MO. REV. STAT. §§ 362.423 through .460, 369.580 through .600, .925 (1969).

lation dealing with foreign banking within their jurisdictions, thereby effectively precluding foreign banks from their territories. Eight states had adopted legislation expressly forbidding foreign banks from establishing banking offices within their territory.[8]

From 1972 until the adoption of the Act, interest and activity on the part of foreign banks in United States operations increased dramatically. During the four-year period ending February 1977, an average of twenty-three facilities per year was opened in the United States by foreign banks, a rate which increased during the next two years, to approximately 56 new facilities per year.[9] Foreign banking activity in California dramatically expanded from June 30, 1970 to June 30, 1979. As of June 30, 1970, there were fourteen agencies and seven subsidiaries (having 49 branch offices) of foreign banks in California. On the same date in 1979, there were seventy-six agencies, one branch, and eighteen subsidiaries (with 435 branches).[10] During the same period, assets of California offices and subsidiaries of foreign banks rose from $1.8 billion in 1970 to more than $32.3 billion in 1979.[11] Not only was there a dramatic increase in the extent of foreign banking business conducted in the United States during the 1970s, but also a shift in the character of the business. In 1972, agencies, which are prohibited from accepting deposits, controlled more than half of the loans, money market assets, securities, and commercial and industrial loans maintained by all foreign banking establishments in the United States; since that time there has been a steady evolution to the branch as the primary banking facility.[12]

The influx of foreign banking institutions during the decade prior to the adoption of the Act is not surprising, considering the expansion of the American economy which had occurred since World War II and the competitive advantages enjoyed by foreign banks in the American market during the period.

Three advantages are of particular significance since they have effectively been eliminated by the adoption of the Act. First, prior to the adoption of the Act, foreign banks were entitled to carry on their banking activities in any state which permitted foreign banking, while American banks were

[8]*See* DEL. CODE ANN. tit. 8, § 379 (1974); MD. CODE ANN. § 12-207 (1980); MINN. STAT. ANN. § 303.04 (WEST 1969); N.J. STAT. ANN. § 17:9A-316 (West 1963); R.I. GEN. LAWS § 19-5-10 (1968); TEX. CONST. art. 16, § 16 (1937); VA. CODE § 6.1-5 (Repl. Vol. 1979); W. VA. CODE § 31A-2-5 (1975).

[9]U.S. GAO Rep., Considerable Increase in Foreign Banking in the United States Since 1972, 4 (1979).

[10]Cal. Supt. of Banks 70th Ann. Rep. 29 (1979).

[11]*Id.*

[12]U.S. GAO Rep., *supra* note 9, at 708; the following table set forth in the GAO Report at page 8 demonstrates the evolution of the type of banking institutions:

restricted by the McFadden Act[13] from operating branches in more than one state. While the wisdom of the prohibition on interstate banking set forth in the McFadden Act continues to be debated, it remains in force, although its effect has been mitigated somewhat by the expanded use of Edge Act Corporations permitted American banks under Section 3 of the Act.[14] The second competitive advantage enjoyed by foreign banks prior to the adoption of the Act was a favorable pricing differential which they were able to offer their customers in competing with American banks since they were not required to pay FDIC insurance premiums nor were they required to maintain federally mandated reserves. Finally, foreign banks enjoyed much more latitude than their American competitors in the scope of the non-banking business they were allowed to conduct prior to adoption of the Act.[15]

These regulatory distinctions have been credited with giving foreign banks the ability to offer a rate differential estimated to have been between 30 and 67 basis points.[16] It has been estimated that the foreign banks' share of the New York market for commercial and industrial loans in 1978 was between 21 percent and 43.4 percent, depending upon the analysis applied.[17] Thus, irrespective of the estimate considered most reliable, it is clear that just prior to the adoption of the Act, the influence of foreign banking establishments in the United States was substantial, whether measured in terms of numbers of facilities, assets or market share.

	November 1972			February 1979		
	Standard banking assets (a)	Commercial and industrial loans	Number of Offices	Standard banking assets	Commercial and industrial loans	Number of offices
	—(percent)—			—(percent)—		
Agencies	55.1	63.1	50	26.2	33.7	144
Branches	18.2	14.2	26	49.5	47.4	124
Subsidiaries	20.7	16.0	25	22.6	17.1	44
Investment companies(b)	6.0	6.7	3	1.7	1.8	6
TOTAL	100.0	100.0	104	100.0	100.0	318

a Standard banking assets include loans, money market assets, and securities. Excluded are balances from related institutions and clearing balances. This concept is considered to be a good measure of a bank's true size.

b Chartered in New York under the New York State Investment Company Act, these organizations finance high risk trade and participate in venture capital schemes.

[13]McFadden Act, ch. 191, 44 Stat. 1224 (1927).

[14]IBA § 3 (amending § 611 of the Edge Act, 12 ULS.C §§ 611-632 (1976), *as amended* by International Banking Act of 1978).

[15]IBA § 8, 12 U.S.C. § 3106 (Supp. II 1978).

[16]*Compare* Bellanger, *The Future of Foreign Banking in the United States or How to Get There (The International Banking Act of 1978 and Beyond)*, 1980, Ill. L. F. 21, 27 (30-40 basis points) (1980) *with* Address by C. Edward McConnell before American Banker's Association International Banking Conference, The Impact of International Banking Activities on Bank Performance, 9 (67 basis point advantage) (January 19, 1979).

[17]McConnell, *supra* note 16 at 7.

After the Act was enacted in September 1978, there was a natural lag in applications to establish branches or agencies under the Act. Notwithstanding the suspicion of the new procedures and the elimination of certain competitive advantages, the Comptroller of the Currency had, by the end of August 1980, approved fourteen applications to establish facilities in the United States[18] and further applications remained on file.

II. Offshore Banking in the Caribbean

In reviewing the Carribbean nations as possible jurisdictions for the establishment of an offshore banking subsidiary to conduct operations in the United States, it is wise to consider both the regulatory attitude and the procedure required to establish the banking subsidiary in the nation chosen.

A. *Regulatory Philosophy*

In general, the Caribbean tax havens' philosophical and regulatory attitudes are deliberately and aggressively tailored to encourage the formation and operation of businesses within their territories. The Caribbean nations are most widely known in the business community for their beneficial tax structures, including both their internal system of taxation and their network of treaty concessions.

The hospitality to foreign banks, however, extends far beyond the tax structure in many of the Caribbean jurisdictions. Many Caribbean jurisdictions have adopted a dual system of bank regulations, under which banks which solicit funds from and make loans to local residents are subject to a customarily stringent set of bank regulations, while the so-called "offshore banks" (which neither solicit funds nor make loans locally) are subject to much less regulation. The lack of supervision in some jurisdictions has led to abuses, in some cases amounting to outright fraud,[19] with a concurrent increase in skepticism for banks from such jurisdictions among bank regulators in banking centers.

In July 1979, Barbados joined other Caribbean nations in creating a dual banking system by adopting its Offshore Banking Act.[20] In order to encourage foreign banks to take advantage of the Offshore Banking Act by locating facilities in Barbados, Prime Minister Adams of Barbados and Dr. Courtney Blackman (Governor of the Central Bank of Barbados) made a promotional trip to New York.[21] While Barbados will not exercise extensive regulatory control over the offshore banks, it will attempt to regulate the quality of banking institutions by careful screening of foreign banks seeking offshore banking licenses.[22] The Bank of the Netherlands Antilles,

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[18]U.S. FED. RES. BD. REP., The International Banking Act of 1978, 13 (Sept. 17, 1980).

[19]*See, e.g.*, Drinkhall, *Con Men Are Raking in Millions by Setting Up Own Caribbean Banks*, Wall St. J., Mar. 23, 1981, at 1, col. 1.

[20]Barbados, Offshore Banking Act, § 49, July 26, 1979.

[21]The Wall Street Journal, April 30, 1980, at 24, cols. 1-8.

[22]*Id.*

the Central Bank for that nation, "still welcomes new banking institutions, but . . . has become more selective . . . [looking] for reputable names."[23] As a routine practice, the Bank of the Netherlands Antilles delivers to each applicant for an offshore banking license a set of guidelines in furtherance of the "aim to avoid that the name of the Netherlands Antilles be compromised as a location of off-shore working credit institutions. . . ."[24]

The practice and policy of carefully screening applicants for banking licenses enunciated by Barbados and the Netherlands Antilles are perceived by those nations as being essential to preserving the integrity of their respective banking communities. As will be seen below, even the most careful scrutiny may not satisfy the Comptroller of the Currency of the United States.

In addition to establishing a dual banking system, Caribbean jurisdictions further seek to encourage foreign banking enterprises to locate in their territories by imposing rather stringent bank secrecy laws, making it possible for banks located there to protect client confidences. For example, the Confidential Relationships (Preservation) Law of the Cayman Islands was adopted because the relevant provisions of the "Banks and Trust Companies Regulation Law has not proved an adequate vehicle for the purpose for which it was formulated and unresolved doubts exist as to its proper interpretation."[25] That law (which carries a sanction of imprisonment for two years or a fine of $5,000 or both for a violation) prohibits the disclosure of bank information in virtually all circumstances. The new Cayman law goes so far as to require that a trial in which a witness is asked questions which could lead to the disclosure of confidential information be adjourned so that the witness may receive a direction from a Judge of the Grand Court sitting alone and *in camera* with respect to the rendering of such testimony.[26]

Barbados has similarly provided for complete banking secrecy by agreeing that it will not solicit information with respect to customer accounts and it will prohibit information from being communicated to anyone other than Barbados officials.[27] The banking ordinance in the Netherlands Antilles prohibits disclosure of confidential information provided to an official and restricts the use of such information to purposes "strictly necessary for the

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[23]H. BEERS, AN INTRODUCTION TO THE FINANCIAL SYSTEM OF THE NETHERLANDS ANTILLES, 44 (1980) (published by the Bank of the Netherlands Antilles). As of November 1980, the Netherlands Antilles had chartered offshore banks with parent banks in the Netherlands, Venezuela, the United States, Canada, the United Kingdom, Switzerland, Italy, France and Abu Dhabi. BEERS, at 78-79.

[24]Letter from the Bank of the Netherlands Antilles (November 8, 1975, Off-Shore Credit Institutions).

[25]Cayman Islands, Confidential Relationships (Preservation) Law, Law 16 of 1976, September 8, 1976, 2.

[26]Cayman Islands, Confidential Relationships (Preservation) Law (Law 16 of 1976), as amended, by the Confidential Relationships (Preservation) (amendment) Law, 1979 (Law 26 of 1979), §§ 3A, 4(i).

[27]Barbados, Offshore Banking Act, § 49, July 26, 1979.

discharge of his function."[28] Although there is no other general bank secrecy law in the Netherlands Antilles, both the authorities and bank officials are strictly enjoined to maintain client confidences. "Requests from foreign authorities [for banking information] will be refused, except when the customer agrees to the disclosure."[29]

A foreign financial institution seeking to establish operations in the Caribbean is, thus, presented with the apparently appealing regulatory picture of tax haven status and complete confidentiality coupled with a simplified application and regulatory process for offshore banks.

B. *Procedure for Establishing an Offshore Bank*

The procedure observed in the Netherlands Antilles is not materially different from those employed in other Caribbean jurisdictions either in the licensing or the regulatory procedures. In order to be licensed as an offshore bank in the Netherlands Antilles, one should arrange to meet preliminarily with representatives of the Bank of the Netherlands Antilles in order to brief them with respect to the character of the applicant institution and with respect to its offshore banking plans. While this procedure is not required, it will greatly facilitate the processing of the application in view of the increasing selectivity of the Central Bank in the granting of offshore banking licenses. After the preliminary meeting, it will be necessary to adopt the Deed of Incorporation before a Civil Law Notary as is required for any Netherlands Antilles corporation.[30]

In drafting the Deed of Incorporation, adequate attention must be paid to the capital structure. The Central Bank will not grant a Declaration of No Objection to a banking institution which employs the so-called "80-20" capital structure, which enables the shareholder to withdraw virtually all of the assets from a Netherlands Antilles corporation under certain circumstances.[31] In addition, consideration must be given to other capital-related factors in the decision, such as the legal lending limit which is made applicable to United States branches of foreign banks by the Act.[32] If any of the managing directors to be appointed under the Deed of Incorporation will be citizens of jurisdictions other than the Netherlands Antilles, it will be necessary to obtain a director's license for each of them. After issuance of the Deed of Incorporation, it must be submitted to the Minister of Justice for approval,[33] entered in the Commercial Register of the Chamber of Commerce[34] and published in the Official Gazette.[35] Prior to commencing

[28]Netherlands Antilles, National Ordinance No. 138, June 26, 1972, containing regulation of the supervision of banking and credit institutions [hereinafter cited as the Banking Ordinance], § 12.

[29]BEERS, *supra* note 22, at 85.

[30]Netherlands Antilles, Commercial Code, Article 33(2).

[31]BEERS, *supra* note 22, at 43.

[32]IBA § 4(b), 12 U.S.C. § 3102(b) (Supp. II 1978).

[33]Netherlands Antilles, Commercial Code, Article 38(1).

[34]Netherlands Antilles, Commercial Code, Article 40.

[35]Netherlands Antilles, Commercial Code, Article 39.

banking operations, the banking subsidiary must apply to the Central Bank for a Declaration of No Objection.[36] The application is customarily in the form of a letter addressed to the Central Bank providing the Central Bank with sufficient information for it to evaluate the reliability, solvency, expertise, structure and proposed operations of the applicant. The Declaration will customarily provide the applicant with six months within which to commence banking activities after issuance. Finally, the offshore bank should apply to the Central Bank for a license exempting it from the foreign exchange controls of the Netherlands Antilles.[37] Upon satisfaction of the steps enumerated, the newly created Netherlands Antilles offshore bank is in position to commence its operations.

The differences in regulatory attitude do not stop when a Netherlands Antilles bank has received permission to commence operations. For example, a local bank (as distinct from an offshore bank) cannot reduce its capital, engage in mergers, acquisitions, or reorganizations, or establish branch offices without permission from the Central Bank.[38] Similarly, local banking organizations are subject to supervision, examination, and reporting requirements, in most cases.[39] Section 14 of the Netherlands Antilles Banking Ordinance expressly exempts from those restrictions and procedures offshore banks "that exclusively make it their business to grant credits abroad from [their] own and/or foreign means, both [of which must have been] obtained from abroad. . . ."[40]

As a result of its concern for the reputation of the Netherlands Antilles in the world banking community, the Central Bank has been considering various enhanced reporting and supervision requirements applicable to offshore banks. The proposed changes would subject offshore banks to conditional licenses (subject to being withdrawn in the event unsound banking procedures or other problems exist), supervision by the Central Bank and increased auditing procedures, in addition to other enhanced regulatory procedures.[41] While such requirements might, at first blush, appear to be onerous and to discourage foreign banks from establishing offshore subsidiaries in the Netherlands Antilles, if properly structured, such changes could be quite beneficial, particularly as they would affect the relationships of the subsidiary bank with United States bank regulatory authorities. Indeed, in view of the fact that many offshore banks voluntarily report quarterly to the Central Bank, the burden of reporting would not be materially altered and may be acceptable, particularly in view of the potential benefit to be gained from submitting to supervision and examination procedures which conform more nearly to those required in banking center countries.

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[36]Banking Ordinance, *supra* note 28, at § 4(1).
[37]Netherlands Antilles, National Ordinance on Foreign Exchange (1940).
[38]Banking Ordinance, *supra* note 28, at § 4(2).
[39]*Id.* at §§ 5-11.
[40]*Id.* at § 14.
[41]BEERS, *supra* note 22, at 44-45.

III. Impact of the International Banking Act

In observing the application of the Act to the Caribbean offshore banking subsidiary, it will be helpful to examine, as a preliminary measure, the policies and legislative history of the Act, the options and procedures for establishing a U.S. facility under the Act, and certain operational features of the Act.

A. *Policy*

The United States has historically had a dual system of bank regulation. National banks were subject exclusively to federal regulation while state banks were subject to state regulation and, depending upon choices made by the bank with respect to membership in the Federal Reserve System and insurance of deposits, they could also be subject to federal regulation. There has never been a uniform system of regulations applied to banks throughout the United States and, while the Act makes some strides in that direction, it carefully preserves intact the dual system of banking.

The cornerstone of the Act's philosophy is that of "national treatment," i.e., a philosophy of insuring that foreign banks doing business in the United States are entitled to the same benefits and subject to the same restrictions as American banks doing business under the same circumstances. The Senate Committee on Banking, Housing and Urban Affairs enunciated the policy as follows:

> The general policy of the United States with regard to foreign enterprises doing business in the United States has been one of national treatment. Under this policy, foreign enterprises operating in the host country are treated as competitive equals with their domestic counterparts. There is, at this time, no uniform national policy concerning foreign banking operation in this country. As a result, foreign banks enjoy many competitive advantages over our domestic banks. [The Act] establishes the principle of parity of treatment between foreign and domestic banks in like circumstances.
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> The climate in which [The Act] has been considered is one of relative calm. Foreign banks doing business in the United States have behaved in a responsible manner, and their presence has been a benefit to the banking industry as a whole. Enactment of a rational framework of Federal Regulation at this time is appropriate and will serve to avoid future problems while enhancing the competitive environment.[42]

The concept of national treatment, however, is a very complex one. It involves not only insuring that foreign banks enjoy no competitive advantage,[43] but also insuring uniform treatment of state and federally chartered banks and a uniform treatment of banks geographically dispersed through-

[42] S. Rep. No. 1073, 95th Cong., 2d Sess. 2, *reprinted in* [1978] U.S. Code Cong. & Ad. News 1421, 1422.

[43] *See* text at note 16, *supra*.

out the United States.[44] At least one commentator has taken the position that the limitations imposed on foreign banks operating in the United States under the Act (particularly with respect to multi-state branching and non-banking activities) may upset previously existing stability and discourage operations in the United States, at least outside of the major banking centers.[45] The degree of discouragement with respect to specific geographical locations must also consider the impact of imposition of reserve requirements depriving foreign banks of their previously enjoyed pricing advantage.

Notwithstanding the criticism which has been leveled at the Act, it has created a relatively rational and simple framework pursuant to which foreign banks may enter the United States market and a coherent philosophy against which the statute may be tested.

B. *Legislative History*

Early in the 1970s American bank regulatory authorities recognized the need for a uniform system of simplified bank regulatory procedures in the United States; consequently, in 1972, the Board of Governors of the Federal Reserve System created a Steering Committee on International Banking which was headed by Vice-Chairman George Mitchell.[46]

After extensive deliberation and revision[47] in both houses of Congress,

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[44]For an analysis of the success of the Act in achieving "national treatment," *see* Feinman, *National Treatment of Foreign Banks Operating in the United States: The International Banking Act of 1978*, 11 L. & POL'Y IN INT'L. BUS. 1109 (1979).

[45]Note, *The Regulation of Foreign Banking in the United States after the International Banking Act of 1978*, 65 U. VA. L. REV. 993, 1028 (1979).

[46]H.R. REP. NO. 95-1073, 95th Cong., 2d Sess. 1 (1978).

[47]As a result of recommendations made by the Steering Committee, the Foreign Bank Act of 1975 (S. 958) was introduced on March 5, 1975, at the request of the Board of Governors. *See* H.R. REP. NO. 95-1073, 95th Cong., 2d Sess. 1 (1978). The Subcommittee on Financial Institutions of the Senate Committee on Banking, Housing and Urban Affairs held hearings on the bill in January 1976. *See Foreign Bank Act of 1975; Hearings on S. 958 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. (1976). On July 29, 1976, the International Banking Act of 1976 (H.R. 13211) was passed by a voice vote in the House of Representatives. 122 CONG. REC. H. 7937-7966 (daily ed., July 29, 1976). The Financial Institutions Subcommittee held hearings on the House version on August 31, 1976; *International Banking Act of 1976; Hearings on H.R. 13876 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. (1976); but the Senate took no further action on either bill prior to adjournment of the 94th Congress; H.R. REP. NO. 95-1073, 95th Cong., 2d Sess. 1 (1978). On May 23, 1977, Committee Chairman Reuss and Subcommittee Chairman St. Germain were joined by 19 other members of the Subcommittee on Financial Institutions in sponsoring the introduction of H.R. 7325, the International Banking Act of 1977, a bill intended to resurrect the initiative of the Board of Governors which had expired with the adjournment of the prior Congress. *See* 123 CONG. REC. H. 4816-4819 (daily ed., May 23, 1977). The Subcommittee held hearings on H.R. 7325 in July 1977; *International Banking Act of 1977: Hearing of the Subcomm. on Financial Institutions, Regulation and Insurance of the House Comm. on Banking, Finance and Urban Affairs*, 95th Cong., 1st Sess. (1977); and in October made substantive amendments to the bill, after which the bill was passed by the Subcommittee by a vote of 16 to 2; Transcript: *Hearings of the Subcomm. on Financial Institutions, Regulation and Insurance of the House Comm. on Banking, Finance and Urban Affairs, mark-up*

the Act was signed into law by President Carter on September 17, 1978. Of particular interest in the legislative history is the degree of importance attached to the passage of the Act by the Board of Governors of the Federal Reserve System and, as will be noted below, some of the specific amendments to the Act proposed by the Board.[48] The effect, if not the purpose, of the Board's proposed amendments is to render it more difficult for a major international bank properly to employ a Caribbean subsidiary to conduct its operations in the United States. The requirement, now set forth in Section 4 of the Act, that an applicant for authority to establish a Federal branch be engaged "directly in a banking business outside the United States,"[49] fails to recognize the viability of a subsidiary of a major international bank created for the purpose of entering the American market.

C. *Available Options for Establishment of Facilities*

After the decision is made to enter the United States banking market it will next be necessary to determine the form the facility will take. The decision will be influenced by a variety of factors, including the market (retail, wholesale or specialty) to be served; the degree of management and reporting autonomy to be granted; the political objectives (e.g., avoidance of identification with one jurisdiction or the impact of currency exchange regulations) to be attained; and the tax benefits (e.g., avoidance of potentially adverse federal income tax requirements to allocate deductions among a bank's worldwide activities or the impact of unitary state income taxes by use of a subsidiary) to be realized.

Before the Act was adopted, a foreign bank, although it could have invested in an Edge Act corporation, could control only one federally authorized entity: a national bank organized as a subsidiary of the foreign institution. America's dual system of state and federal licensing of banks left substantial latitude. Of the ten (or eleven) states which authorized foreign banking entities to carry on business within their territories, seven ostensibly permitted the use of either agencies or branches: Alaska, Cali-

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of H.R. 7325 (Oct. 11-12, 1977, available at House Banking Comm. office). On February 9, 1978, a clean bill, H.R. 10899, the International Banking Act of 1978, which reflected the actions taken by the Subcommittee, was introduced; 124 CONG. REC. H. 944 (daily ed., Feb. 9, 1978). The Full Committee on Banking Finance and Urban Affairs again amended the bill and by a vote of 46 to none ordered the bill favorably reported. H.R. REP. No. 95-910, 95th Cong., 2d Sess., 10 (1978). The bill passed the House in April 1978; 124 CONG., REC. H. 2551-2575 (daily ed., Apr. 6, 1978); was marked-up again; Transcript: *Senate Comm. on Banking, Housing and Urban Affairs, mark-up of H.R. 10899* (July 26, 1978, available at Senate Banking Comm. office); and passed by the Senate on August 15, 1978. 124 CONG. REC. S. 13387-13396 (daily ed., Aug. 15, 1978).

[48] *See* letter from Chairman Arthur F. Burns to Chairman Fernand J. St. Germain May 25, 1977 reprinted in *International Banking Act of 1977; Hearings before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Comm. on Banking, Finance and Urban Affairs*, 95th Cong., 1st Sess. 101-134 (1977) [hereinafter cited as Burns' letter].

[49] IBA § 4, 12 U.S.C. § 3102(a) (Supp. II 1978).

fornia, Illinois, Massachusetts, New York, Oregon, and Washington.[50] The remaining four jurisdictions permitted only agencies to be established within their boundaries. It should be noted, however, that while California ostensibly permitted foreign branches to engage in business in the state, the requirement of FDIC insurance effectively precluded branches from being established. Foreign banks were permitted to operate agencies (which could accept no deposits from local residents, but did engage in the full range of banking activities) and branches (which ordinarily provided a full range of banking activities). Foreign banks also established representative offices, which were not authorized to engage in banking business but merely serve as a sales and promotional facility for the foreign bank. Finally, the foreign banks were authorized to establish subsidiaries in many states, since the subsidiaries were to be domestic banks rather than foreign banks, without regard to offshore ownership. As is discussed below, the same range of alternative forms for carrying on business exists under the Act and, indeed, it has been expanded to include comparable forms at the federal level.

The Act, in preserving the dual system of banking regulation, leaves in place the option of organizing a branch, agency or subsidiary under the laws of one of the fifty states, even though that branch, created under the Act, will have greater federal regulation than would have heretofore been the case. Analysis of the comparison between state and federal licensing alternatives is beyond the scope of this work; however, the factors to be considered in making the election between state and federal facilities has been the subject of careful analysis.[51] Even within the federal licensing authority, a wide variety of alternatives continue to exist: the National Bank, as a subsidiary; the Edge Act corporation, as a subsidiary; the branch or agency authorized by the Act[52] (either directly or through an offshore subsidiary); and the representative office. The cost, complexity and competitive disadvantages in establishing a newly created national bank in the United States, particularly in view of the restrictions imposed on such a bank,[53] are such as to make it abundantly clear why so many foreign institutions have expressed an interest in acquiring or have actually acquired existing banks in this country rather than forming new banks. Conversely, the desirability of formation of an Edge Act corporation is substantially diminished by the restricted nature of activities permitted to an Edge Act corporation.[54] Even if the potentially desirable alternatives of formation of a national bank, an Edge Act corporation or a representative office are

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[50]*See* statutes cited at note 5, *supra*.

[51]Glidden and Shockey, *U.S. Branches and Agencies of Foreign Banks: A Comparison of the Federal and State Chartering Options*, 1980 U. ILL. L. F. 65 (1980).

[52]IBA § 4, 12 U.S.C. § 3102(a) (Supp. II 1978).

[53]*E.g.*, the directors must, in the absence of a waiver obtained from the Comptroller of the Currency, all be citizens of the United States and two-thirds of the directors must reside within 100 miles of the bank. 12 U.S.C. § 72. Those conditions may be unacceptable to a foreign bank interested in establishing operations in the United States.

[54]Edge Act, *supra* note 14.

rejected, the number of alternatives available to a foreign bank interested in participating in the United States market remains considerable.

A foreign bank interested in doing business in the United States must first decide whether to do business in its own name or to form a subsidiary. The considerations affecting this decision are the traditional ones (market, management considerations, political factors, and taxation) referred to above. Either the foreign bank, in its own name, or a banking subsidiary, e.g., one organized in a Caribbean tax haven, may, under appropriate circumstances, establish a facility in the United States with the permission of the Comptroller of the Currency.[55] If, for the reasons enunciated, the foreign bank elects to form a banking subsidiary in a Caribbean jurisdiction, e.g., the Netherlands Antilles, it still may elect to open its U.S. facility as an agency or one of three levels of branches. An agency may engage in a full range of asset-side banking activities and may maintain credit balances incidental to its banking powers; however, it may not accept deposits from United States citizens or residents.[56]

An alternative to the agency for the establishment of a United States facility is the so-called limited federal branch referred to in Section 5 of the Act.[57] The limited federal branch is restricted in that it can only receive deposits which are permitted to be received by an Edge Act corporation.[58] The principal advantage of a limited federal branch over an Edge Act corporation is the ease with which the powers of the limited federal branch can be enhanced to those of a full branch, thereby giving it substantially increased deposit-taking powers at an appropriate time in the branch's existence. Indeed, it is currently anticipated that an application to "upgrade" a limited federal branch to full branch status (without FDIC

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[55]IBA § 4(a), 12 U.S.C. § 3102(a) (Supp. II 1978).

[56]IBA § 1(b)(1), 12 U.S.C. § 3101(1) (Supp. II 1978).

[57]IBA § 5, 12 U.S.C. § 3103(a) (Supp. II 1978).

[58]An Edge Act corporation may receive the types of deposits permitted to it under Regulation K, 12 C.F.R. Part 211 which provides, in pertinent part, as follows:

> 1) Deposits from foreign governments and persons. An Edge Corporation may receive in the United States demand, savings, and time deposits (including negotiable certificates of deposits) from foreign governments and their agencies and instrumentalities, persons conducting business principally at their offices or establishments abroad, and individuals residing abroad.
>
> 2) Deposits from other persons. An Edge Corporation may receive in the United States demand, savings, and time deposits (including negotiable certificates of deposits) if such deposits:
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> i) Are to be transmitted abroad;
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> ii) Consist of collateral or funds to be used for payment of obligations to the Edge Corporations;
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> iii) Consist of the proceeds of collections abroad that are to be used to pay for exported or imported goods or for other costs of exporting or importing or that are to be periodically transferred to the depositor's account at another financial institution;
>
> iv) Consist of the proceeds of extensions of credit by the Edge Corporation; or
>
> v) Represent compensation to the Edge Corporation for extensions of credit or services to the customer.

12 C.F.R. § 211.4(e).

insurance) can, assuming no unforeseen problems arise, be processed by the Office of the Comptroller of the Currency in less than two months.

The third form which a United States facility of a foreign bank may take under the Act is that of a full, federally insured branch. The insured branch may engage in a full range of banking activities (except for the exercise of fiduciary powers, for which authority must be separately sought) and, consequently, is in a position to compete with local banks for both retail and wholesale banking business. A foreign bank with branches in the United States may have a full branch in only one state (the bank's "home state") although the bank may operate limited federal branches outside its home state to the extent permitted by the Act.[59] The costs associated with the increased deposit-taking power possessed by a full branch are principally the costs imposed in conjunction with obtaining FDIC insurance. Those costs include the making of an asset pledge for the protection of the deposit insurance fund,[60] semi-annual payment of an annual assessment roughly equivalent to an insurance premium as required by Section 7(c) of the Federal Deposit Insurance Act,[61] and the asset maintenance, reporting, and examination requirements imposed generally on FDIC-insured institutions. In addition, to the extent that a full branch receives deposits of less than $100,000, it becomes subject to the interest rate limitations specified in Regulation Q[62] and to the provisions of the Community Reinvestment Act of 1977.[63]

As a final alternative, it is possible for a foreign bank to operate a full branch in the United States without having its deposits insured by the FDIC, provided it complies with certain restrictions regarding the taking of deposits in amounts of less than $100,000.[64] A bank which does not propose to accept retail deposits may, by satisfying regulatory requirements,[65]

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[59] IBA § 5, 12 U.S.C. § 3103 (Supp. II 1978); Regulation K, 12 C.F.R. § 211.22.

[60] 12 C.F.R. § 346.19.

[61] 12 U.S.C. § 1817(c).

[62] 12 C.F.R. § 217.

[63] 12 U.S.C. §§ 2901 *et seq.*

[64] 12 C.F.R. § 28.8.

[65] 12 C.F.R. § 28.8(a) provides that a full branch which accepts initial deposits of less than $100,000 only in accordance with the requirements of 12 C.F.R. § 346.6(a) need not obtain insurance. Section 346.6(a) provides, in pertinent part, that uninsured initial deposits of less than $100,000 may be received from the following:

> 1) Any business entity, including any corporation, partnership, association or trust, which engages in commercial activity for profit, provided that this category excludes any business which is organized under the laws of any State or the United States, is majority owned by United States citizens or residents and has total assets of less than $1,500,000 at the most recent fiscal year statement as of the date of initial deposit. The $1,500,000 asset test is applicable to the depositor's combined financial interests including the business activities of an individual or parent company and its majority owned subsidiary(s).
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> 2) Any governmental unit, including the United States government, any State government, any foreign government and any political subdivision or agency of the foregoing.
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> 3) Any international organization which is comprised of two or more nations.
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> 4) Any depositor who established deposit account on or before September 16, 1979 at a branch established before September 17, 1978 and who has continuously maintained the

void the burdens imposed on FDIC insured institutions. The deposit-taking powers of a full, but uninsured federal branch are quite extensive, and may satisfy the bank's marketing objectives, particularly in view of the fact that most foreign banks entering the United States markets are principally interested in wholesale, rather than retail, banking activities. If, however, the full branch wishes to accept retail deposits beyond those specified, it must apply to the Comptroller for permission to do so or obtain FDIC insurance of its deposits.

From the foregoing, it is apparent that a foreign bank entering the United States market has quite a broad range of alternatives open to it: from the representative office, for which the only requirement under the Act is to register,[66] to the formation of a wholly-owned national bank as a subsidiary, which is subject to the entire scope of United States banking regulation. Even within the range of vehicles authorized expressly by the Act, there is substantial latitude. The only constraints are the business purposes of the bank establishing the facility and the requirements of state law in the jurisdiction in which the facility will be located.[67]

D. *Procedure for Establishment and Operation of Agencies or Branches under the Act*

In order to open an office in the United States, a foreign bank must apply to the Comptroller of the Currency for permission, in accordance with the provisions of Section 4(a) of the Act, which provides as follows:

> Except as provided in Section 5 [12 U.S.C. § 3103], a foreign bank which engages directly in a banking business outside the United States may, with the approval of the Comptroller, establish one or more Federal branches or agencies in any State in which (1) it is not operating a branch or agency pursuant to State law and

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deposit account since the September 1979 date, provided that the provisions of this paragraph (4) shall be effective only until September 16, 1982.

5) Any other depositor but only if (i) the amount of deposits under this paragraph (5) does not exceed on an average daily basis 4% of the branch's deposits for the last 30 days of the most recent calendar quarter, excluding deposits in the branch of other offices, branches, agencies or wholly owned subsidiaries of the bank and (ii) the branch does not solicit deposits from the general public by advertising, display of signs or similar activity designed to attract the attention of the general public. A foreign bank which has more than one State branch in the same State may aggregate deposits in such branches (excluding deposits of other branches, agencies or wholly owned subsidiaries of the bank) for the purpose of this paragraph (5).

The average shall be computed by using the sum of the close of business figures for the last 30 calendar days ending with and including the last date of the calendar quarter divided by 30. Calculations as to the average shall be retained by the branch until the next examination.

6) Any draft, check or similar instrument for the transmission of funds issued by the bank.

7) Any depositor who is not a citizen of the United States and who is not a resident of the United States at the time of the initial deposit.

12 C.F.R. § 346.6(a).

[66] Act § 10(a), 12 U.S.C. § 3107(a) (Supp. II 1978); 31 C.F.R. Part 123.

[67] Act § 4(a), 12 U.S.C. § 3102(a) (Supp. II 1978).

(2) the establishment of a branch or agency, as the case may be, by a foreign bank is not prohibited by State law.

The procedures for submission of the application are specified in 12 C.F.R. §§ 4.7(c) *et seq*. A filing fee of $2,500 is payable at the time the application is submitted. The application required by the Comptroller is relatively straightforward and is divided into four parts. Part A, which is required of all applicants, sets forth general information about the foreign bank. Part B is, itself, divided into three portions, the first of which is required in all applications and calls for a description of the business to be carried on at the U.S. facility. The second portion is required of applicants for agencies and branches not accepting retail deposits, while the third portion is required only of branches accepting retail deposits. Part C is required only of banks accepting retail deposits and is an application to the GDIC for deposit insurance. Part D is an application for authority to exercise fiduciary powers at a federal branch. Depending upon the completeness of the information at the time of original submission, the Office of the Comptroller of the Currency can process the application in relatively little time. In granting approval of the application, the Comptroller will require acknowledgment that the branch will comply with applicable United States law and will, in addition, require the establishment of a Capital Equivalency Deposit, as required by Section 4(g) of the Act. The amount of the Capital Equivalency Deposit must be at least the larger of the amount of capital which would be required of a national bank being established at the same location or 5 percent of the total liabilities of the branch or agency including acceptances but excluding accrued expenses and amounts due to affiliates of the foreign bank.[68] The Capital Equivalency Deposit is an independent requirement from the reserve requirements of Regulation D or the asset maintenance requirements for FDIC insurance (although the amount is considered in determining the latter).

After receiving notification of the preliminary approval by the Comptroller of the Currency of the establishment of the branch and satisfaction of all the conditions specified therein, including establishment of the Capital Equivalency Deposit, the federal branch may commence its operations. The Act imposes some interesting restrictions on operating activities of the newly established branch.

With certain specified exceptions, the obligations to a licensed federal agency or branch from any person (or affiliated group of persons) may not exceed 10 percent of the bank's fully paid capital and unimpaired surplus.[69] Under the Act, the legal lending limit has been applied to all branches and agencies of a foreign bank; however, the limit is based on the capital structure of the bank as a whole, including its foreign operations. In addition, the legal lending limit, obviously, has no applicability to obligations

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[68]IBA § 4(g)(2), 12 U.S.C. § 3102(g)(2) (Supp. II 1978).

[69]12 U.S.C. § 84 and regulations adopted pursuant thereto.

incurred outside of the United States, a fact which lends itself to interesting syndication transactions among branches of the same institution.

One of the principal instruments for carrying out monetary policies extended to the Federal Reserve Board is the ability to impose minimum reserve requirements for various classes of deposits on member institutions.[70] A branch or agency of a foreign bank in the United States is required to comply with generally applicable reserve requirements set forth in the Federal Reserve Act, as amended, and Regulation D as though such office were a member of the Federal Reserve System, if its parent foreign bank has (a) total worldwide assets in excess of $1 billion or (b) is controlled by a foreign company or a group of foreign companies that own or control foreign banks which in the aggregate have worldwide consolidated bank assets in excess of $1 billion.[71] Most U.S. branches, even if they are branches of Caribbean subsidiaries of major foreign banks will, consequently, be subject to reserve requirements. A newly organized federal branch operating in the United States must pay careful attention to the requirements of Regulation D, as revised, effective November 13, 1980, which contains provisions specifically dealing with U.S. operations of foreign banks.[72]

A United States branch or agency of a foreign bank is subject to a broad range of reporting obligations, consistent with the concept of national treatment. The Federal Reserve Board has, however, implemented a reporting system for banks operating under the Act which have generated substantial controversy. When, on October 29, 1979, the Board proposed adoption of Form F.R. Y-7 (the annual report of foreign bank holding companies),[73] the proposed form generated a storm of criticism not only among foreign banking institutions, but also among foreign bank regulators. The form, as initially proposed, purported to require disclosure of information at least arguably required to be maintained in confidence under the home jurisdiction's bank secrecy laws and, purported to require disclosure of information which, if not required to be kept secret, was certainly confidential information with respect to the business activities of affiliates of the foreign bank. The foreign bank regulators concluded that the proposed reporting requirements ran contrary to the position taken by the United States in the 1975 agreement among the Group of Ten and Switzerland that primary authority for regulating and supervising the affairs of banks must rest with the central banking authorities in their home jurisdiction. The Bank of England, in commenting on the proposal, said:

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[70]Federal Reserve Act, 12 U.S.C. §§ 221 *et seq.*, as amended by the Monetary Control Act of 1980, Title I of Pub. L. No. 96-221, 94 Stat. 132 (March 31, 1980), and Regulation D adopted pursuant thereto, 12 C.F.C. § 204.

[71]IBA § 7(a), 12 U.S.C. § 3105(a) (Supp. II 1978).

[72]*E.g.*, 12 C.F.R. § 204.2(h) (45 Fed. Reg. 56009, August 22, 1980).

[73]44 Fed. Reg. 64906 (1979).

> These proposals appear to us to carry with them an implication that the U.S. authorities consider it necessary to extend their regulatory jurisdiction into the affairs of non-American banks. We could find this a troublesome principle and one which if generalized would materially damage effective international cooperation in this field.[74]

In response to the storm of criticism, the Federal Reserve Board substantially modified the proposed reporting form in its final adoption;[75] however, substantial confidential information is still required and it remains to be seen what the reaction of the world banking community to the required reporting obligations will be. In separating the final reporting form into multiple parts, some of which are to be retained in confidence, the Federal Reserve Board may have gone far enough to satisfy foreign bank regulators; however, the degree of extraterritoriality seems likely to offend many capable foreign bank regulators.

IV. Regulatory Problems under the Act

In addition to the problems inherent in complying with any newly adopted regulatory statute, three areas of concern arise in the context of using a Caribbean banking subsidiary to enter the United States under the Act. They are: (i) the requirement of Section 4(a) that a foreign bank must be engaged "directly in a banking business outside the United States" before it can be licensed under the Act; (ii) the extent of the examination and supervision accorded offshore banks by Caribbean jurisdiction and the attitude of the Federal Reserve Board with respect thereto; and (iii) the apparent conflict between the foreign jurisdiction's bank secrecy laws and the reporting requirements of the United States Treasury Department.

The Federal Reserve Board has adopted a very rigid view of the "directly engaged" requirement, which was added to the Act at the request of the Federal Reserve Board. Irrespective of the size, banking experience or reputation of the parent of a newly created offshore banking subsidiary, that subsidiary must itself comply literally with the requirement of Section 4(a) of the Act that it be "engaged directly" in a banking business.

As originally proposed in H.R. 7325, Section 4(a) did not include that requirement and provided, in pertinent part:

> Except as provided in Section 5, a foreign bank may, with the approval of the Comptroller, establish a federal branch or agency in any State in which (1) it is not operating a branch or agency pursuant to State law and (2) the establishment of a branch or agency, as the case may be, by a foreign bank is not prohibited by State law.[76]

In addition, the definition of "foreign bank" contained in H.R. 7325, as originally proposed, provided as follows:

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[74]American Banker, November 10, 1980.

[75]46 Fed. Reg. 12110 (1981).

[76]H.R. 7325, 95th Cong., 1st Sess. § 4(a) (1977).

> "Foreign bank" means any institution that (1) organized under the laws of a foreign country, a territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands and (2) either (a) principally conducts its banking business outside the United States or (b) is a subsidiary, as that term is defined in the Bank Holding Act of 1956, of any institution which, on a consolidated basis, principally conducts its banking business outside the United States.[77]

In reviewing the pending legislation, the Federal Reserve Board took the position that the definition of "foreign bank" as embodied in the bill was excessively restrictive, resulting in the exclusion from regulation of "shell banks" for which regulation was rational in view of the scope of the Act.[78] The Board proposed an amendment to the definition of the "foreign bank" to prevent a result considered objectionable by the Federal Reserve Board, i.e., "if a group of individuals chartered a bank in the Cayman Islands and that bank in turn established U.S. branches and agencies, it would not be covered by the Act."[79] The purpose of the amendment to the definition was to insure that the scope of the Act be broad enough to reach all entities seeking to establish operations in the United States pursuant to the Act. The Federal Reserve Board went on to suggest that "[w]ith respect to the particular provisions of the Act, it is left to the agencies to adopt, if needed, other definitions of the term as may be appropriate to carry out the provisions of the Act or prevent evasion thereof. This gives flexibility to consider the purposes of each provision and to tailor the definition as needed."[80]

While it is perfectly rational for the Board to be concerned about the ability of a newly created "shell" bank to enter the United States banking market without being subject to regulation, the very flexibility to which the Board alluded indicates that a rule of reason should be applied in viewing the provision of Section 4(a) as adopted to permit the establishment of a Caribbean banking subsidiary for the sole purpose of carrying on activities in the United States under the Act so long as the parent shareholder of the Caribbean subsidiary is a sufficiently viable and responsible institution willing to guarantee the obligations of its newly created subsidiary.

While most foreign banks using Caribbean subsidiaries to enter the United States will probably want the offshore branch to engage in Eurocurrency transactions and to participate in transactions which would otherwise exceed the United States' legal lending limits, a bank which does not desire to have the offshore branch transact business in this way should not be precluded from receiving the benefits of the Act in the form desired. Similarly, the newly created subsidiary should not be compelled to commence its operations in the Caribbean prior to opening in the United States if the effect is to severely dislocate developmental plans. This is particularly true where, as will often be the case, there will be no permanently assigned

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[77] H.R. 7325, 95th Cong., 1st Sess. § 1(b)(7) (1977). Burns's letter, *supra* note 59 at 115.

[78] *See* Burns's letter, *supra* note 59 at 115-16.

[79] *Id.* at 115.

[80] *Id.* at 115-16.

personnel in the Caribbean jurisdiction. By viewing the applicant bank on a consolidated basis, the statutory provision can be rationalized in a way which does not adversely affect the interests of major international financial institutions interested in entering the United States market and, at the same time, does not permit evasion by the less qualified institutions.

A second series of problems is created by the apparently beneficent attitude of the Caribbean jurisdictions which do not extensively supervise or examine the affairs of offshore branches created in their territories. Since the United States and the remainder of the Group of Ten have concluded that examination and supervision are the principal responsibility of the bank regulatory authority in the home jurisdiction,[81] the attitude of the Comptroller of the Currency and the Federal Reserve Board in expecting foreign regulators to exercise substantial control over the offshore activities of a foreign bank with U.S. branches is not unreasonable. This is particularly the case when United States regulators are precluded by bank secrecy laws from obtaining information with which they can satisfy themselves of the safeness and soundness of the foreign bank's overall condition. The attitude of the Bank of the Netherlands Antilles in reconsidering the desirability of examining and supervising the affairs of offshore banks organized in that jurisdiction appears to be a step in the right direction. Until the Caribbean jurisdictions are willing and able to exercise supervisory authority over offshore banks organized under their laws, it will be necessary for those institutions to persuade the Comptroller of the Currency and the Federal Reserve Board that adequate examination and supervision of the offshore activities of the bank are being undertaken by responsible bank regulatory authorities. Under certain circumstances, regulatory authorities can be "hired" to conduct examinations which they would not otherwise be required to conduct. In the long run, the preferable course would appear to be the amendment of the banking laws of many Caribbean jurisdictions to require or permit an offshore bank organized under their laws to consent to (and to pay for) the examination by and supervision of bank regulatory authorities in the home jurisdiction.

The final unusual problem confronting a Caribbean subsidiary seeking to enter the United States market is created again by the apparently beneficial bank secrecy laws prevalent in the Caribbean jurisdictions. The Federal Reserve Board and the Comptroller of the Currency are of the view that, without regard to foreign supervision and examination, it will be necessary for the foreign bank operating a facility under the Act to report to the United States authorities in great detail. The Federal Reserve Board recently enunciated the reasons for the reporting requirements:

> These proposals are designed, first of all, to provide adequate disclosure on the financial operations of the foreign bank, on a world-wide basis. This information will enable the Board to analyze the parent organization's ability to be a continu-

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[81] *See* text, *supra* at note 74.

> ing source of strength to the banking operations being conducted in the United States. Second, they are intended to provide early indications of possible abuse of United States banking operations by a weak or troubled foreign bank. Third, the reporting requirements have been formulated to provide information on the United States nonbanking activities of foreign banks to determine compliance with the applicable nonbanking prohibitions of the Bank Holding Company Act.[82]

At least until such time as arrangements can be made between United States bank regulatory authorities and those of other jurisdictions, it will be necessary to report substantial amounts of confidential information with respect to foreign activities and individuals (including foreign reserves considered highly secret by foreign bank regulatory authorities) to American bank regulators. The objective sought by the Federal Reserve Board certainly does not deviate from the goals of bank regulators abroad. Each seeks a sound worldwide banking community operated with the least governmental interference consistent with ensuring soundness and legality. The Federal Reserve Board has made substantial strides in insuring exemption from the Freedom of Information Act for certain information required to be filed with the Federal Reserve Board. Regulatory authorities in foreign jurisdictions should take the next step in accommodating worldwide banking interests of major institutions by amending their laws to permit waiver of certain provisions of the bank secrecy laws upon organization of a bank in their jurisdiction, at least to an extent sufficient to permit compliance with U.S. reporting requirements. Adoption of such provisions would make the waiver elective with the institution and, thereby, enhance the viability of the multi-national banking network.

V. Conclusion

The use of banking subsidiaries organized in tax haven jurisdictions as vehicles for establishing branches and agencies in the United States pursuant to the Act will, in many cases, be highly desirable for business, political and economic reasons. The procedures to be followed are, in no case, overly complex. However, the procedures would be greatly facilitated by the adoption of a rule of reason by the Federal Reserve Board in viewing applicants under Section 4(a) of the Act on a consolidated basis; by the expansion of the regulatory and supervisory authority of Caribbean bank regulators (at least on a voluntary basis) with respect to offshore banks; and by the modification of bank secrecy laws in the Carribbean jurisdiction and disclosure requirements in the United States.

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[82]U.S. FED. RES. BD. REP., The International Banking Act of 1978, 27 (Sept. 17, 1980).