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INTERNATIONAL CORPORATIONS
OF
AMERICAN BANKS

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C.

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PREFACE

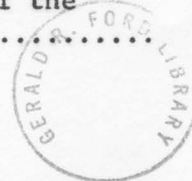
The analyses and conclusions set forth are those of the writer and are based solely on his independent study of the subject. They do not purport to represent an expression or reflection of the opinions or policies of the Board of Governors, of the Federal Reserve Banks, or of members of their staffs.

Allen F. Goodfellow



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CHAPTER I

INTRODUCTION

As a general rule banks that are members of the Federal Reserve System are not permitted to hold the stock of other corporations. Among the few exceptions are the stocks of certain corporations which supplement and augment the international banking and financial operations of the banks. These corporations accomplish this through several different methods, but there are two which stand out as being the most significant. First, they can, in effect, breach the ban on branching across State lines, insofar as it applies to strictly international operations. Secondly, these corporations have the power, with supervisory consent, to purchase and hold the stock of foreign or international companies.

The need for this additional flexibility in international banking operations has become increasingly apparent to the banks during the sharply accelerating growth of these operations which began in the late 1950's. The result has been a remarkable growth in the number, size, and variety of utilization of these corporations. Thus far this growth in the utilization of these corporations has shown no sign of abating.

One of the strange things about these corporations and the rapidity of their recent growth is that they are not newcomers to the international banking scene. The legislation making possible their use by the banks was actually enacted some 50 years ago. Furthermore, within 10 years of the initial legislation no fewer than 18 had come into existence. Yet, in another 10 years their number had dropped to five and there were still only 6 by 1954.



This uncertain background, contrasted with the current growth and breadth of their utilization make these corporations an interesting facet in today's international operations of American banks. While the principal purpose of this paper is to set forth and analyze the present functions and future prospects of these corporations, it is necessary to first understand their legal basis and something of their earlier history. Thus, the statutory authority, regulatory history, and supervisory actions relating to these corporations is explored in the following Chapter. Then, after a relatively brief review of their earlier history, their current operations and functions are analyzed in some detail. Next, there is an investigation of some of the problems which they have encountered or have raised, and finally there is an attempt to glimpse into what their future may hold.

As will be detailed in the following pages, there are two types of these international corporations whose stock can be held by banks that are members of the Federal Reserve System. These corporations are known as Agreement Corporations and Edge Corporations. Henceforth, these two types of corporations will be referred to jointly as Corporations, except where they need to be referred to separately, in which case the above names will be used.



CHAPTER II

STATUTORY, REGULATORY AND SUPERVISORY AUTHORITY AND ACTIONS

The statutory authority for national banks and, since the Banking Act of 1933, for State banks that are members of the Federal Reserve System¹ to hold stock in the Corporations is found in Sections 25 and 25(a) of the Federal Reserve Act. The responsibility for the regulation and supervision of these corporations is placed with the Board of Governors of the Federal Reserve System. In fulfilling its regulatory function the Board of Governors has issued Regulation K - "Corporations Doing Foreign Banking or Other Foreign Financing Under the Federal Reserve Act."

Statutory Authority

Prior to the enactment of the Federal Reserve Act in 1913 there was no statutory authority for national banks to establish foreign branches, create acceptances, or hold the stock in corporations engaged in international banking and financing.² One of the many purposes of the original Federal Reserve Act was to broaden and strengthen the international operations of the national banks and hence it included provisions authorizing the first two of these activities. However, it made no provision for the third type of international operation.

¹"United States Banking Organization Abroad," Federal Reserve Bulletin, December, 1956, p. 1234.

²Banking Organization Abroad, p. 1236.



Section 25 - Amendment of September 7, 1916³

This amendment to the Federal Reserve Act was the outgrowth of renewed interest in banks being able to undertake operations abroad through subsidiaries. This was considered of particular importance for the smaller banks which did not have the capabilities of undertaking foreign branch operations themselves, but could participate with others through this corporate device.

This amendment permits banks, under certain conditions, to invest in the stock of corporations "principally engaged in international or foreign banking, or banking in a dependency or insular possession of the United States, either directly, or through the agency, ownership, or control of local institutions in foreign countries, or in such dependencies or insular possessions." The corporation can be chartered either by the Federal or State governments, but no provision is included in this Section for the Federal chartering of corporations.

The conditions under which such stock holdings are permitted are that the bank have a capital and surplus of \$1 million or more, that it invest no more than 10 per cent of its capital and surplus in such stock, that it receive the permission of the Board of Governors of the Federal Reserve System, and that the corporation enter into an agreement or undertaking with the Board of Governors. In this last, the corporation has to agree "to restrict its operations or conduct its business in such manner or under such limitations and restrictions as said Board may prescribe." It is because of the requirement for an agreement that the corporations operating under this Section have come to be known as "Agreement Corporations."

³12 United States Code 601-604a. See Appendix 4, pp. 10-12.



Section 25(a) - December 24, 1919⁴

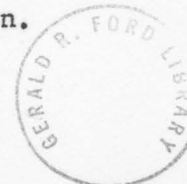
As already noted the 1916 amendment to Section 25 did not provide for Federal chartering of these international Corporations. Due to this omission there were continued efforts to enact such a provision. These finally resulted, some three years later, in the addition of Section 25(a) to the Federal Reserve Act. The legislation which created this new Section was sponsored by Senator Edge of New Jersey, and therefore it has been called the "Edge Act" and the corporations chartered under it have been known as "Edge Corporations."

Since this Section provides for the actual chartering of corporations it is a far more intricate statute than its predecessor. It spells out in considerable detail the organization and powers of these Edge Corporations. However, a basic understanding of its provisions can be attained if one focuses on two aspects of the Edge Corporations: first, the manner in which they differ from the Agreement Corporations, and second, the specific restrictions that are imposed by statute on their operations.

There are a number of differences between the Edge Corporations and the Agreement Corporations, some of which are of considerable importance and others merely of passing interest. The principal ones are the following:

1. The Edge Corporation is Federally chartered and not subject to corporation or banking laws of the States, while the Agreement Corporation is normally chartered under and subject to State laws.
2. The Edge Corporation must have a minimum capital of \$2 million, while there is no minimum for the Agreement Corporation.

⁴12 U.S.C. 611-631. See Appendix 4, pp. 12-22.



Since a parent bank is limited in both cases to investing a maximum of 10 per cent of its capital and surplus in the stock of these Corporations, to have an Edge subsidiary requires that a bank have a minimum of \$20 million in capital and surplus, whereas only the statutory minimum of \$1 million is necessary for a bank to have an Agreement subsidiary.

3. The majority of the shares of an Edge Corporation must be owned by citizens of the United States, or legal entities controlled by such citizens, and all directors must be citizens, while there are no equivalent restrictions on Agreement Corporations.

4. All national and State member banks are by statute authorized to invest in the stock of an Edge Corporation, whereas they must receive the approval of the Board of Governors to invest in the stock of an Agreement Corporation.

5. Edge Corporations are "organized for the purpose of engaging in international or foreign banking or other international or foreign financial operations . . .", whereas Agreement Corporations must be "principally engaged in international or foreign banking . . .". Thus, the operations of the Edge Corporation may specifically include "other international or foreign financial operations" while those of the Agreement Corporation apparently are confined to banking. However, the Agreement Corporation need only be "principally engaged" in such activities, whereas no such leeway is granted the Edge Corporation, having been specifically removed during its passage through Congress.⁵

⁵Banking Organization Abroad, p. 1283.



The statutory restrictions on the operations of the Edge Corporations pertain primarily to operations in the United States. No Edge Corporation is permitted any activity in the United States "except such as, in the judgment of the Board of Governors of the Federal Reserve System, shall be incidental to its international or foreign business." They can receive "only such deposits within the United States as may be incidental to or for the purpose of carrying out transactions in foreign countries or dependencies or insular possessions of the United States...." Furthermore, they cannot purchase and hold the stock of any company which deals in merchandise or commodities in the United States, nor of any company which transacts any business in the United States except, such as the Board of Governors finds "may be incidental to its international or foreign business. . . ."

Other statutory restrictions include a limitation on the issuance of bonds and debentures, a minimum reserve on deposits received in the United States, and a prohibition on engaging in "commerce or trade in commodities" or attempting to control or fix prices of commodities. The statute also restricts the amount that a Corporation can invest in any one stock, but permits exceptions to this when approved by the Board of Governors.

Regulation K⁶

This regulation is issued under the broad discretionary authority granted the Board of Governors of the Federal Reserve System (hereafter the Board) in the enabling statutes and now applies to all operations of

⁶12 Code of Federal Regulations Part 211, Regulation K - Corporations Doing Foreign Banking or Other Foreign Financing Under the Federal Reserve Act. See Appendix 4, pp. 1-9.



both Edge and Agreement Corporations. Neither Section sets forth extensive guidelines or standards and both leave the supervision of the Corporations primarily at the discretion of the Board.

Basis of the Board's Authority

Prior to 1957 the Regulation dealt only with the Edge Corporations, so that it was in this context that the Board's regulatory posture in this regard was developed.

While Section 25(a) refers in several places to "rules and regulations" of the Board, the basic statutory authority for Regulation K is found in the preamble to the listing of the powers of the Corporations:

"Each corporation . . . shall have power, under such rules and regulations as the Board . . . may prescribe: . . ."

As previously noted a few specific limitations or requirements of an operational nature are established by the statute. However, the vast majority of supervisory policy and detail is left to the discretion of the Board with the purpose of the Edge Corporations--international banking and financing--and two general statutory standards being its only guidelines.

The first of these standards is related to the authorization for the Board to add to the Edge Corporations' powers abroad, and sets forth the guides to such additional powers. This statutory provision is found at the end of the principal listing of these Corporations' powers, and states:

". . . and generally to exercise such powers as are incidental to the powers conferred by this Act or as may be usual, in the determination of the Board . . . , in connection with the transaction of the business of banking and other financial operations in the countries, colonies, dependencies, or possessions in which it shall transact business and not inconsistent with the powers specifically granted herein."



The second is that which establishes the standard for the limitations on the Edge Corporations' activities in the United States:

"No corporation . . . shall carry on any part of its business in the United States except such as, in the judgement of the Board . . ., shall be incidental to its international or foreign business . . ."

Under Section 25, the Board originally exercised its supervisory power solely through the individual agreements and amendments thereto. In general, these agreements, and the amendments to them, paralleled the requirements of the Revision of Regulation K then in effect, at least to the extent that such requirements were relative to the Agreement Corporation concerned.

Finally, in the 1957 and 1963 Revisions of Regulation K, the operations of the Agreement Corporations were brought within the purview of that Regulation. The pertinent statutory provisions of Section 25 are the following:

"Before any national bank shall be permitted to purchase stock in any such corporation the said corporation shall enter into an agreement or undertaking with the Board . . . to restrict its operations or conduct its business in such manner or under such limitations and restrictions as the said board may prescribe for the place or places wherein such business is to be conducted. . . . Should . . . investigation result in establishing the failure of the corporation in question . . . to comply with the regulations laid down by the said Board . . . national banks may be required to dispose of stockholdings in the said corporation upon reasonable notice."



Historical Development of Regulation K

Neither the relevant portion of Section 25 nor Section 25(a) has been basically altered since their original enactment in 1916 and 1919, respectively. Because of this the alterations in the Regulation and agreements have resulted either from changes in the Board's approach or its response to the changing and expanding operations of the Corporations. A knowledge of the historical development is of assistance in understanding the underlying policy problems, the considerations relating

thereto, and the development of the Board's posture in relation to them. This is true even though the development of Regulation K has not been particularly evolutionary in character, except for the last two major Revisions, namely, those of 1957 and 1963.

1920-1954.⁷ The original version of Regulation K was issued in March 1920, and there were subsequent revisions or amendments in 1924, 1927, 1928, 1930, 1943, 1945, and 1954. Aside from their being largely a repetition of the statute, the most striking thing about these earlier versions is their lack of emphasis on those functions of the Corporations which today are the most utilized. Not a single version dealt in detail with the Corporation's operations in the United States, but all merely repeated the general wording of the statutory limitations. Likewise, while there were a number of changes relating to the acquisition of stocks by the Corporations, they appear to have been only a reflection of philosophical changes in the Board's basic approach to the Regulation as a whole, rather than any particular concern with the exercise of this power.

The first version of the Regulation was understandably primarily concerned with the chartering, naming, and establishment of the Corporations. Subsequently, in 1927, a considerable portion of the Regulation dealt with the issuance of bonds and debentures, provisions which saw little if any utilization by the Corporations. The fact that these two subjects continued to constitute virtually two thirds of the Regulation throughout this period, would seem to indicate an absence

⁷While only the Regulation is referred to, the agreements followed the same general pattern.



of any serious problems with the Corporations' operations, or perhaps a lack of operations, and hence experience, on which to base more detailed revisions of the Regulation.

Throughout this period there seems to have been a basic philosophical, or practical difference in views as to whether it was proper to allow the Corporations a limited freedom in certain operations or whether they should always be required to obtain the Board's approval. This difference appears to have extended even as to whether the Regulation should provide for the Board to make exceptions to certain regulatory limitations or prohibitions. Illustrative of these are the three absolute reversals in the provision of the Regulation relating to the acquisition of stocks and the changes relating to the names of Corporations and the limitations on aggregate liabilities.

The original Regulation of 1920 permitted stock acquisitions without prior Board consent, except where the statute itself required Board approval. In the 1924 Revision, Board consent was required in all instances. In 1927, the provision reverted to the position of the original version and finally in 1943 prior Board consent was again required for all acquisitions.

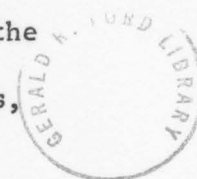
The 1928 version of the Regulation stated that the name of a Corporation could not include the word "bank" and must contain either the word "international" or "foreign." In 1930 the provision was added that the Board could waive these requirements. The limitation on aggregate liabilities similarly shows the differences in view as to whether the Regulation should provide for exceptions to be granted by the Board. In the 1920 version provision was made for Board approval of a Corporation's exceeding the regulatory limit on aggregate liabilities. This provision was removed in 1927 and reinstated in 1945.



As stated earlier, the history of Regulation K does not present any clear picture of evolutionary development, particularly in these early years. While an amendment to a provision on one type of operation might give the Corporations a greater freedom or flexibility, other changes often moved in the contrary direction in relation to other operations. Furthermore, either, or both, changes were not infrequently reversed by subsequent amendments. However, viewing the Regulation as a whole, there was a gradual movement toward allowing the Corporations an increasing degree of freedom and flexibility in their operations, both directly and through provisions for Board approval of exceptions to the regulatory restrictions.

1957 Revision. This version of the Regulation was fundamentally the outgrowth of the general resurgence of interest in international operations by American banks following the end of World War II. Various overseas military facilities were opened, former foreign branches reopened, and other new ones established. Also in the future was the glowing potential of full fledged international banking operations, should the major currencies once again become convertible.

Not too far from the beginning of this epoch there was established in New York a newly organized Corporation called Bank of America, a wholly-owned subsidiary of Bank of America National Trust and Savings Association, San Francisco, the largest bank in the world. This Corporation immediately launched into an active and extensive international banking business, including a large amount of deposit and loan activity. As discussed in the preceding section, Regulation K's only references to such operations in the United States were at this time still couched in the rather vague language of the statute. This lack of clarity raised



innumerable regulatory and supervisory problems in relation to the new Corporation. These were further compounded by questions regarding other Corporations acquiring stock and generally entering into an investment banking business.

As a result of these developments, the Board of Governors appointed a committee to review the entire field of operations of the Corporations, both actual and potential. This committee was composed of members of the Board's staff and officers of several of the Federal Reserve Banks. Since the committee's report dealt to a large extent with the then present or contemplated operations of the Corporations it is discussed in greater detail in the succeeding Chapter. Suffice it to say at this point that this report, submitted in November 1954, was a dominating factor in many of the provisions of the Revision which became effective January 15, 1957.

In general, the 1957 Revision represented a considerable change from the earlier versions which were largely a repetition of the statutory language with only a few additions and interpretations. While this Revision still repeated much of the statutory phraseology it also contained extensive interpretations and innovations. The most significant changes wrought by the 1957 Revision were: the creation of two types of Corporations, Banking and Financing; the establishment of specific restrictions and limitations on operations in the United States; the provision for Financing Corporations obtaining limited general consents for the purchase of stock in foreign companies; and the inclusion of Agreement Corporations within the purview of the Regulation.



Earlier versions of the Regulation had made certain distinctions between those Corporations which received deposits and those that did not. These usually limited only the exercise of the power to issue bonds and debentures. The 1957 Revision, however, created a sharp separation between commercial and investment banking, thus following the philosophical distinction set forth in the banking legislation of the 1930's. Banking Corporations were permitted to take deposits and create acceptances, but were limited in underwriting, were prohibited from issuing bonds and debentures, and their stock acquisitions were usually restricted to those of foreign banks and bank related companies. On the other hand, Financing Corporations were prohibited from accepting deposits, creating acceptances and ordinarily from acquiring stocks in companies engaged in banking. This division of the functions of the Corporations, particularly as relates to stockholdings, caused the creation of "twin" Corporations which are discussed in Chapter IV.

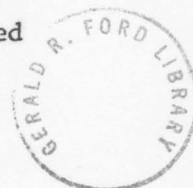
A considerable portion of the 1957 Revision of the Regulation was concerned with the various permissible and prohibited operations in the United States. It detailed various operations in both categories as related to each the Banking and the Financing Corporations. For example, Banking Corporations could ordinarily receive a deposit from a foreign depositor, except where it was to be used in paying expenses of an office or representative in the United States. Many of these detailed regulatory requirements resulted from earlier experience arising out of the Board's examinations of the Corporations. Their being set forth in such detail has proven to be an aid, both to the Corporations and to the Board's examiners and staff.



In the preceding section we have already seen how, prior to 1957, the regulatory provisions for the acquisition of shares of stock had swung between the two extremes of requiring a specific consent for all acquisitions and granting a blanket consent, except where the Board's approval was required because of size. Since 1943 the former rule had been in effect. While the 1957 Revision basically continued this approach, it did provide that Financing Corporations could obtain from the Board a limited general consent to acquire stock that fell within a proposed program. This concept of a limited general consent is important in understanding the development of the Regulation, not only because it established a third position between the earlier extremes, but also because out of it grew the subsequent provisions for the General Consent that appeared in the Revision of 1963.

As mentioned earlier, this Revision included the Agreement Corporations within its purview for the first time. However, the Agreement Corporations were restricted to those activities permitted Banking Corporations, this seemingly being based on the fact that Section 25 makes no reference to such corporations being engaged in international finance.

1963 Revision. The repetition of the statutory language, including the specific limitations in the Act, virtually disappeared from this Revision. Its various provisions were basically limited to matters of a purely regulatory nature based on interpretations of the statutory language. Additionally, it had an introductory section on the national purpose of the Act. Despite this extreme change in format, the 1963 Revision was in substance only a further development and refinement of the 1957 version. At the time that the 1957 Revision was formulated, the policy was established that it should be reviewed in five years,



taking into consideration the experience gained in the meanwhile. The current Regulation was the outgrowth of just such a review, and from the substantive point of view incorporated only two fundamental changes: the abolition of the formal distinction between the Banking and Financing Corporations, and the creation of the regulatory General Consent.

The current Regulation provides for but one type of Corporation, which may engage in both banking and financing operations of an international character. However, as was done in all prior Revisions, it does retain certain special restrictions or limitations on the operations of those Corporations "engaged in banking." Thus, where aggregate demand deposits and acceptance liabilities of a Corporation exceed its capital and surplus it is restricted in the underwriting of securities and has a lower limit on the liabilities of one borrower.

There was considerable rewording of the interpretive provisions relating to a Corporation's deposits, loans and other activities in the United States and whether or not they are to be considered "incidental to its international or foreign business." However, these changes were primarily of a drafting nature, the principal substantive refinements being restricted to (1) the elimination of prime commercial paper as a permissible means of temporarily employing funds, (2) the permitting of the subsequent acquisition of loans which could have been financed at inception, and (3) the removal of the requirement for permissible deposits that an individual residing abroad be a "foreign national."

Next to the abolition of the two types of Corporations, the most important change in the 1963 Revision was the incorporation into the Regulation itself of a General Consent for the acquisition of certain



stocks. As already mentioned, a provision for the Board's approving applications for a limited general consent for Financing Corporations was included in the 1957 Revision. However, by its terms this provision did not apply to Banking Corporations and, hence, did not extend to stock in foreign banks and, furthermore, the specific general consents granted under this provision were all limited to stock in non-financial companies. In the 1963 Revision all Corporations were permitted to acquire stock of a foreign company if (1) it was in connection with an extension of credit, (2) represented less than a 25 per cent interest in a foreign bank, or (3) was a small - not over \$200,000 - investment that was likely to further United States foreign commerce. In general, this provision was considerably more flexible than the earlier one.

With the inclusion of a General Consent in the Regulation, one other addition was also made, which is worthy of note. Prior to the 1963 Revision, the Board's grants of consent to acquire stocks had evolved to the point where they always contained certain conditions. These required that the Corporation dispose of the stock of any company that (1) engaged in buying or selling goods in the United States or undertook any other activity in the United States not incidental to its international business, (2) engaged in the business of underwriting or distributing securities in the United States, (3) or undertook any other operation which the Board should find made a continued stock holding by a Corporation inappropriate. In the new Revision the second and third of these conditions were incorporated into the text of the Regulation itself, as conditions to all acquisitions of stock, whether by specific or General Consent. In line with the general format of the Regulation, the first condition was omitted since it was nothing more than a restatement of a clear statutory limitation.



The 1963 Revision of Regulation K also continues the inclusion of Agreement Corporations within its purview as was first done in 1957. They are subject to the same statutory and regulatory restrictions⁸ as Corporations chartered under Section 25(a) which are "engaged in banking."

Since the issuance of the 1963 Revision, the Regulation has been amended once to bring it into conformity with the new provisions of Regulation M which provided for the acquisition of foreign bank stock by national banks.⁹ This amendment deleted those parts of Regulation K relating to the examination of foreign subsidiaries and to the maximum liability of Corporations and their subsidiaries to parent banks.¹⁰

Supervision

Besides its responsibility for the issuance of Regulation K, the Board also has supervisory responsibilities, arising either directly from the statutes or from the Regulation. Certain operations of the Corporations require specific Board approval and the Board also has the overall responsibilities of supervising the activities of the Corporations.

To help in fulfilling these responsibilities the Board has a number of supervisory tools. In granting its approval - or consent - the Board may do so unconditionally, or may feel it advisable to do so only

⁸Except these relating to their organization.

⁹12 CFR Part 213, Regulation M, "Foreign Activities of National Banks."

¹⁰Due to balance-of-payments considerations, it was again amended effective February 8, 1968. This amendment removed the General Consent provision in Section 211.3(a). "Press Release," Board of Governors of the Federal Reserve System, February 8, 1968.



subject to certain limitations or conditions. In discharging its more general supervisory responsibilities the Board's specific tools are those of examination and of requiring reports. Finally, for the general guidance of the Corporations - short of regulatory changes - the Board may issue interpretations. Such interpretations usually arise from specific applications or supervisory examination problems where the subject matter is of broad or general interest.

Applications

The applications for Board approval cover a variety of subjects, but one stands out as by far the most numerous and also as raising the more difficult questions, namely requests for consent to purchase shares of stock. Other applications, some of which are of a routine nature, include requests for increases in capital, for amendments to Articles of Association, for branches, for permission to exceed regulatory limitations, for reversal of examiners' findings and conclusions, and possibly for the issuance of bonds, although no Corporation has made such an application in recent decades.

Conditional Consents

Many requests for permission to acquire and hold shares of stock in a given company can be of a fairly routine nature. However, others can raise troublesome questions as to the propriety of such a holding due to the type of business involved, the political situation in the country, operations conducted in the United States, the degree of control involved, or any combination of these factors. The more difficult situation is where a holding is considered by the Board to be appropriate only in certain circumstances. In such cases the Board has granted its consent to the acquisition subject to certain conditions. As



mentioned in regard to Regulation K, two of the earlier conditions were found to be of such common application that they were incorporated into the 1963 Revision.

Since the issuance of the 1963 Revision the Board's consent to the acquisition of minority stock interests has usually not been subject to any conditions. The exceptions to this rule have been where the company concerned was operating in the United States. In this regard the operations of a subsidiary of the foreign company have been considered to be those of the parent.

The statute itself sets forth one specific class of activities in the United States which makes the holding of stock by a Corporation prohibited, namely, dealing in merchandise or commodities. Furthermore, all other activities in the United States must be incidental to the company's foreign or international business. The general premise, on which the Board has acted in attaching conditions to consents, is that, for a Corporation to hold stock in a company, the company generally must not transact any business in the United States which is not permissible for the Corporation itself.

The acquisition of stock which represents control of a company raises parallel, but slightly different problems. The stock in all subsidiaries for which the Board has granted its consent is held by the Corporations subject to conditions which in essence place the subsidiaries in the same position as their parent. Thus, the Corporation cannot continue to hold the subsidiary's stock unless the operations of the subsidiary conform to the same restrictions and limitations as are imposed by the statute and regulation on the operations of the Corporation itself. One specific exception to this is the limitation on loans



when made in the local currency of the country where the subsidiary operates. Since the amendment to Regulation K of March 15, 1967, deleting the requirement that a Corporation cause any subsidiary to submit to examination by the Board, the parallel condition in consents has not been used. However, the conditions still require that the Corporation file such reports on subsidiaries as the Board may require. To date these have consisted of reports on acquisitions and dispositions of stock and semi-annual reports of condition.

Examinations and Reports

The principal supervisory tools that the Board has for keeping it abreast of the activities of the Corporations are those of examination and of requiring reports. Each Corporation is examined annually and the report thereon is reviewed by the Board's staff. While foreign subsidiaries are not examined, it has been expected that the parent Corporation will have on file such information as is necessary to its own supervision of any subsidiary.¹¹ Thus far this information has proven adequate for the purposes of the Board's examination of the Corporation's overall activities.

The Board also receives semi-annual Reports of Condition from each Corporation, covering its own financial position, and also those of any controlled subsidiary. At least one of the two reports received each year contains schedules of the principal accounts, giving further breakdowns as to currencies involved, affiliated relationships, etc.

¹¹See "Press Release," Board, March 15, 1967, p. 3-4.



Additionally, a report is received quarterly showing all acquisitions and dispositions of stock by the Corporation and its subsidiaries. Where basic information regarding the company invested in has not previously been supplied to the Board, such data is included in the quarterly report.

Interpretations

Thus far there have been only four Board interpretations dealing with the Corporations.¹² Of these, two have involved questions relating to Corporations engaged in banking, i.e., purchase and sale of Federal Funds, and the manner of calculating deposits for aggregate liabilities. Only one has had to do with a stock acquisition by a Corporation. In that case it was found appropriate, based on the particular facts, for a Corporation to hold a noncontrolling interest in a company acting solely as a combination export manager in the United States. Besides these published interpretations, a few Board decisions in the past have been circulated to all or some of the then operating Corporations.

Agreements

Prior to the Revision of 1957 the Board exercised its supervision of the Agreement Corporations primarily through the original and amended agreements with those Corporations, the approvals required therein, and through examinations and reports. The earlier agreements were usually tailored to the needs of each Corporation and, hence, had a considerable degree of variation. Gradually there evolved a single

¹²Interpretations of the Board of Governors of the Federal Reserve System, Chapter 18, pp. 481-2. One interpretation, regarding subsidiary banks of Bank Holding Companies having a Corporation, has been deleted from publication as it is no longer relevant due to a change in the statute.



basic pattern which paralleled the general requirements of Regulation K. Since that Regulation was revised to bring these Corporations within its purview, the new agreements and amendments to older agreements have generally been confined to the Corporation's acceptance of the Regulation as controlling.



CHAPTER III

THE EARLY YEARS - 1916-1954

A glimpse of the Corporations and their activities in these earlier years is helpful in establishing perspective for the subsequent study of their current activities.

Prior to 1930¹³

Eighteen Corporations came under the Board's jurisdiction during these years, 3 of which were Edge Corporations and 15 were Agreement Corporations. However, of the 18 only 3, all Agreement Corporations, survived beyond the early Thirties. One of these dropped its agreement in 1947 and one converted to an Edge Corporation in 1957.

The lack of success of these earlier Corporations appears to have been due to a number of factors. First and foremost was probably the general lack of experience in foreign banking and financing. This lack of experience affected not only the parent or participating banks' approach and attitude toward the Corporations' operations, but also the availability of capable personnel. Aggravating this inexperience was the economic crisis of 1920-21 and the instability of world prices that followed. The difficulties of the Corporations were further compounded as some of the banks themselves undertook many of the functions that the Corporations had been fulfilling.

¹³The source of most of the data in this section is "United States Banking Organization Abroad," Federal Reserve Bulletin, December 1956, p. 1284, et seq.



Ownership

Of these 18 Corporations only 5 originated as wholly-owned subsidiaries and 3 of these were owned by the same bank. All of the others had multiple ownership and the stock of 1 was sold to the public. In most cases the stockholders consisted of several American banks, but in 3, foreign banks also had an interest, and several had industrial or other financial companies as stockholders. Additionally, there were two instances where 1 Corporation held some of the stock of another Corporation. As time passed a number of the multi-owner Corporations became wholly-owned subsidiaries and others sold all or parts of their business - principally foreign branches - to other Corporations, to American banks, or in one case to a foreign bank.

Operations

The early Corporations generally emphasized operations abroad, either through direct branches or through subsidiaries. Of the 18 Corporations 8 maintained foreign offices, ranging from a single representative office to 21 branches, and at least 6 had foreign banking or financial subsidiaries. While only 2 concentrated their activities on international banking operations in the United States, 6 had financing or investment operations in this country. All but 3 of the Corporations maintained their head office in New York, but 8, principally those with overseas branches, also maintained 1 or more other offices in the United States.

1930-1948

This period of world depression and world war saw an overall decrease in the international activities of American banks. Nonetheless, there were formed during this time three Corporations, one Edge and two



Agreement. Each was established for a fairly specific purpose, to take over foreign branch operations in two cases, and to act as a holding device for the stock of an English trustee company in the other. All three were still in existence at the end of 1954, which is when the following Chapter takes up the recent growth and operations of the Corporations. There was one casualty during this period, however, when in 1947 one of the earlier Agreement Corporations cancelled its agreement with the Board when the American banks sold their interests.

1949 - Bank of America

The formation of this Corporation is in some ways a connecting link between the earlier and more recent periods of utilization of the Corporations. Since it had opened eight foreign branches before they were transferred to its parent in 1963, it could be said to form an epilogue to the typical operations of the earliest Corporations. However, this network of branches developed under special circumstances and never played the dominant role in the Corporation's basic function as did the branches of the 1920's. Bank of America's basic function was the establishment of a New York presence for its Pacific Coast parent. In this it was a forerunner or prologue to the revival of interest in the utilization of this corporate device. Despite Bank of America's relatively broad scope of operations and rapid growth, which illustrated the Corporation's potential, it was 10 years before another bank established a new subsidiary Corporation and 12 years before another was formed to establish a New York presence for its parent institution.

The Mid-1950's - Prelude to the 1957 Revision

By the mid-1950's the industrial countries of western Europe and Japan were well on the way to recovering from the devastation of World War II. International trade and investment had increased substantially.



Nevertheless, international transactions were still hampered by continued controls on trade and capital movement, and major currencies remained inconvertible. A principal aim of the international economic policy of the United States was the dismantling of this residue of wartime controls and the restoration of currency convertibility, with a view to promoting still further international trade. At the time, however, despite the vast potential of the American banking system it had not yet developed its international activities to the point where they were commensurate with this country's economic stature in relation to the rest of the world. Illustrative of this was the fact that during the postwar period the banks' reported claims on foreigners had remained fairly constant and in the mid-1950's amounted to only about 15 per cent of the amount of short-term liabilities reported by the banks as owed to foreigners.¹⁴

It was in this context that the Board initiated a review of the foreign operations of American banks. This review was made by members of the staffs of the Board and of the Federal Reserve Banks in the Districts most concerned with international trade and finance, and a number of banks and several exporting manufacturers were consulted. The participants included men with backgrounds and experience in law, bank supervision and international economics. This permitted a broad and multi-faceted consideration of the foreign operations of American banks in general and those of the Corporations in particular.

The essential conclusions of this review are reflected in the provisions of the 1957 Revision of Regulation K. These provisions show an

¹⁴In contrast, as of December 31, 1967, the short- and long-term claims on foreigners reported by banks were more than 10 times the earlier amount and over 60 per cent of demand and time deposits reported by banks as due to foreigners. International Capital Transactions of the U. S., Federal Reserve Bulletin, February 1968, pp.A73 and A77.



obvious concern with the relationships of the Corporation's operations and certain traditional characteristics of American banking.

The 1957 Revision contained for the first time a detailed delineation of the deposit and loan activities that could not be carried on by the Corporations in the United States. These delineations represent a balancing between the needs of the Corporations for viable and effective international banking operations, and the traditional decentralization of American banking as epitomized by the rule prohibiting inter-State branching.

Similarly the requirement in the Revision for the formal separation of the Banking Corporations and Financing Corporations was a clear reflection on the Corporations' operations of the philosophy of the Banking Act of 1933 which separated commercial and investment banking.

While these two provisions could be considered as trying to adapt the requirements of an international banking operation to a traditional domestic banking mold with a minimum of distortion, there were other provisions which had more of a tendency to expand and increase the flexibility of the Corporations' international operations and hence those of the parent banks. The Revision emphasized the possible scope of such operations by including in the Regulation for the first time the essence of the statutory provision permitting a Corporation ". . . generally to exercise such powers . . . as may be usual, in the determination of the Board...in connection with the transaction of banking or other financial operations in the countries, colonies, dependencies, or possession which it shall transact business and not inconsistent with the powers



"specifically granted herein" ¹⁵This provision and that for a specific general consent for stock acquisitions by Financing Corporations indicated a desire that the Corporations be utilized in a manner foreseen in the original enactment of the Edge Act, namely to permit American banks to compete more effectively in the international market.

The changes in the Regulation removed much of the vagueness and generalities of the statutory language. In many ways they demonstrated the methods whereby the Corporations could increase the scope and flexibility of the international operations of American banks and help to overcome some of the weaknesses in those operations. These methods were quickly adopted and put to use by the American banking community. Within six years after the issuance of the Revision, more Corporations were formed than in the previous forty years. Furthermore, the scope of their activities was vastly increased.

¹⁵12CFR Part 211, effective January 15, 1957, p.5. A somewhat parallel provision relating to foreign branches of member banks was incorporated in a 1962 amendment to Section 25 of the Federal Reserve Act (12 U.S.C. 601-604a) and the subsequent Revision of Regulation M (Foreign Activities of National Banks, 12 CFR Part 213).



CHAPTER IV

RECENT GROWTH AND UTILIZATION

A revival in the use of the Corporations has formed an integral and essential part of the overall expansion of the international activities of U. S. banks since the mid-1950's. At the end of 1954 there were still only 6 Corporations in existence. By the end of 1967 there were 52 Corporations in operation. This tremendous revival of interest in the Corporations was the result of a new appreciation of their unique powers--powers that were often an essential factor in the expansion of a bank's international operations.

These 13 years have seen not only a large increase in the number of Corporations, but vast changes in their size and range of activities. As already noted, they have also seen two extensive revisions of Regulation K under which they operate. The first 5 years of this period, however, were largely a time of experimentation and adjustment, and there was no widespread increase in numbers or activity. Despite this relatively slow beginning these years were a precursor of the tremendous growth which has taken place during the 1960's.



Growth of the Corporations

The six Corporations in existence at the end of 1954 are shown in Table 1 on the following page. The two Corporations with non-New York parents, First of Boston International Corporation and Bank of America, maintained complete international banking operations in New York, and the latter also had a branch in Duesseldorf, Germany. All operations of Morgan & Cie Incorporated were concentrated at its office in Paris, France, where it conducted a general commercial banking business. Bankers Company of New York acted purely as a holding device for the stock of Bankers Trustee and Executor Co. Ltd., London, England. The remaining two Corporations were generally inactive at the time, although each held some stocks and bonds and each had an inactive overseas office.

The development of the Corporations and their parent banks has naturally been similar to the growth and spread of international banking operations in general. Since the mid-1950's international banking in the United States has had a phenomenal growth. These operations today are not only several times their previous size, but also involve many more banking institutions. Moreover, these institutions are no longer in only a few of the principal trade centers along the coasts but are now spread among most of the major financial centers of the country.



TABLE 1
CORPORATIONS IN OPERATION IN 1954

<u>Corporation</u> <u>(Parent Bank^a)</u>	<u>Year^b</u>	<u>Type</u>
International Banking Corporation (First National City Bank)	1901	Agreement
First of Boston International Corporation (The First National Bank of Boston)	1918	Agreement
The Chase Bank (The Chase Manhattan Bank (National Association))	1930	Edge
Bankers Company of New York (Bankers Trust Company)	1931	Agreement
Morgan & Cie. Incorporated (Morgan Guaranty Trust Company of New York)	1941	Agreement
Bank of America (Bank of America National Trust and Savings Association)	1949	Edge

^aCurrent name.

^bFor Agreement Corporations date of State charter shown, the date of the Agreement often being subsequent thereto.



Paralleling this development of international operations in general, the number of Corporations in operation has increased from the 6 in 1954 to 53 today,^{15^a} and their total capital accounts from \$41 million to almost \$360 million.^{15^b} While in 1954 they were all located in New York, they are today scattered in a dozen cities ranging from Seattle to Los Angeles on the Pacific Coast and from Boston to Miami on the Atlantic, as well as at several interior centers and the Virgin Islands. However, despite this increased geographic spread, New York still remains the predominant center of the Corporations' activities, as is true with international financial operations in general. Thus, the majority of the Corporations are still located in New York, and of the 34 Corporations so situated, 14 are subsidiaries of non-New York City parents.¹⁶

Today, 37 banking institutions,¹⁷ including virtually every major bank conducting international operations, have at least 1 Corporation. In 1954 the 6 banks with Corporations included the 3 largest banks in the country, with all others being among the

^{15^a}As of December 31, 1967, including one not yet opened for business.

^{15^b}As of June 30, 1967.

¹⁶For these purposes Marine Midland Corporation, Buffalo, New York, parent of Marine Midland International Corporation, New York, is considered a New York based parent as its lead bank, Marine Midland Grace Trust Company is located there. Since the end of 1967, one Corporation, a subsidiary of Bank of America National Trust and Savings Association, Bamerical International Financial Corporation, which is not "engaged in banking" was authorized to move from New York to San Francisco. Board of Governors of the Federal Reserve System K.3 1968 No. 7 for the week ended February 24, 1968, "Changes in Corporations Engaged in Foreign Banking and Financing."

¹⁷Including two Bank Holding Companies, the lead bank of which is used in subsequent comparisons as to size.



30 largest. Now the 37 parents include the 18 largest banks in the country and 31 of the 52 largest. In 1967 they also represented every member bank with overseas branches¹⁸ and all banks with a base of over \$100 million under the voluntary foreign credit restraint program. Whereas in 1954 the parents consisted of 4 New York City banks and only 1 each in Boston and San Francisco, today there are 11 New York City based parents¹⁹ and 26 that are situated in 11 cities scattered throughout the country.

The dramatic growth in the utilization of the Corporations over the past dozen years is shown in Table 2 on the following page. The table also shows that the renewal of interest did not really gain momentum until the 1960's, over 10 years after the establishment of Bank of America. While the number of parent institutions increased over six-fold, it was in the single year of 1963 that one-fourth of all present parent institutions first organized an international Corporation. It is also noteworthy that of these nine parents, seven were located outside New York.²⁰ In these dozen years the number of Corporations increased almost nine-fold, their total capital accounts by virtually nine-fold,

¹⁸Only one non-member bank, Bank of Hawaii, has overseas branches, these being situated in U. S. Pacific possessions and Trust Territories.

¹⁹See footnote 16 above.

²⁰Appendix 2 contains a list of the Corporations organized, liquidated, and converted from an Agreement to Edge Corporation for each year since 1954.



TABLE 2

STATISTICS SHOWING THE GROWTH OF THE CORPORATIONS

Year- end	No. of Parents	No. of Corpo- rations	-----(amounts in thousands of dollars)----		
			Total Assets	Equity Holdings (at cost)	Capital Accounts
1954	6	6	\$ 231,916	\$ 2,004	\$ 41,019
1955	9	7	252,654	3,956	52,424
1956	9	7	400,984	3,980	57,688
1957	7	7	429,027	16,002	78,115
1958	7	7	471,572	16,466	79,969
1959	7	9	427,856	20,479	84,826
1960	10	15	550,177	26,353	91,484
1961	10	16	592,950	28,487	98,221
1962	13	27	665,356	48,816	150,059
1963	22	36	635,383	68,992	179,906
1964	25	38	888,672	90,891	200,342
1965	29	42	1,016,142	146,314	254,389
1966	33	49	1,387,604	199,588	311,531
6-30-67	36	51	1,626,176	218,904	359,886
1967	37	53			

See Appendix 3 for the source and bases of these statistics.



and their equity investments over a hundred-fold. In Appendix 1 is a list of the banking institutions that currently have one or more operating Corporations, together with the names and locations of the latter.

Changes in Utilization

Since the mid-1950's there have been a number of areas in which there have been changes and experimentations in the utilization of the Corporations. These include the type of ownership, the Agreement versus the Edge Corporations, the use of "twin" and multiple Corporations, the independent versus the foreign department integrated Corporations, and finally the different operations which various Corporations have undertaken in the overall international business of their parent institutions.

Ownership

Today all of the Corporations in operation are wholly-owned subsidiaries. This is in striking contrast to the experience prior to 1930 when 12 of the 18 Corporations which came under the Board's jurisdiction were originally owned by more than 1 bank. Of these 12, three also had foreign as well as United States banks as stockholders and there was one Edge Corporation whose stock was sold to the public.

Since 1930, 58 Corporations have been established. Of these only 1 had multi-bank ownership, and 1 other was a wholly-owned subsidiary of a non-banking company. The former, American Overseas



Finance Corporation, was formed in 1955 by The Chase Manhattan Bank, Chemical Corn Exchange Bank, The First National Bank of Boston, Mellon National Bank and Trust Company and National Bank of Detroit. One, if not the principal, purpose for its establishment was to extend foreign credits in cooperation with and under the guarantee of the Export-Import Bank. When satisfactory arrangements with that institution proved impractical, several of the shareholding banks desired to withdraw from the operation. Thus in 1957 the business of the Corporation was sold and the Corporation liquidated. The purchaser was American Overseas Finance Company, another Edge Corporation, which was wholly-owned by American Overseas Investing Company, Inc., a New York Corporation, which was controlled by industrial interests. In 1960 the new "AOFC" merged its business into that of an affiliated company and entered liquidation.

The reasons for the lack of success of the earlier multi-bank Corporations have never been clearly documented. However, the principal causes were, at least in part, the same problems that were encountered by all Corporations of that period, namely the highly unstable condition of international trade and the lack of experienced personnel. Regardless of the cause of their lack of success, 6 of the 12 were subsequently taken over by wholly-owned Corporations or by a single bank which incorporated the foreign branches into its own foreign branch network. In another instance the foreign branches were taken over by a foreign bank, The Royal Bank of Canada.



The more recent dissolution of American Overseas Finance Corporation appears to have resulted from its inability to obtain its principal objective of working closely with the Export-Import Bank. However, there may also have been some subtle fears on the part of one or more of the non-New York banks of losing their independence in international operations to their large New York partners.

In any event subsequent efforts toward establishing a multi-bank Corporation have to date been ineffective. When the Fidelity-Philadelphia Trust Company established a Corporation in 1963, it intentionally chose a name, The Company for Investing Abroad, that was not specifically associated with the bank's name, in the anticipation that banks in other parts of the country might join as shareholders. Such expectations were never realized and eventually the Corporation's name was changed to The Fidelity International Corporation, when its parent shortened its name to The Fidelity Bank.²¹

The lack of success of the multi-bank international corporate operations to date is of particular interest in that this was originally considered as one of the prime advantages of this corporate device. It was expected that banks which were unable to maintain a full-fledged international operation by themselves would utilize this device to pool their resources and thus be able to compete with the larger banks and to better serve their customers than could otherwise

²¹Since the end of 1967, The Fidelity Bank, together with Wachovia Bank and Trust Company, Winston-Salem, North Carolina, and Zilkha & Sons Inc., New York, have been authorized to form an Edge Corporation, American International Bank to be headquartered in New York City. Board of Governors of the Federal Reserve System H.2 No. 7 (1968), page 2.



be done by each individual bank. It was apparently these aims which recently moved James J. Saxon, former Comptroller of the Currency and subsequently Co-chairman of American Fletcher National Bank and Trust Company, Indianapolis, Indiana, to recommend that various medium-sized banks throughout the country should join together in forming an Edge Corporation.²²

In discussing multi-bank Corporations, some mention should be made of the anomalous position of those Corporations which are wholly-owned subsidiaries of Bank Holding Companies. In many ways such Corporations are in a position to serve a number of banks in their international operations, not only through overseas contacts and relationships, but perhaps more particularly in serving the non-New York banks through having the head office of the Corporation in New York. On the other hand, these holding companies and their subsidiary banks can be regarded as a single banking institution which has taken this particular form due to the laws relating to branch banking. Thus far, there have been three Corporations owned by Bank Holding Companies and all have been located in New York City.²³

²²An application by American Fletcher National Bank and Trust Company to form an Edge Corporation was received in early November 1967, but has not yet been acted on. Board of Governors of the Federal Reserve System H.2 No. 44, (1967), page 3.

²³Since the end of 1967, United Virginia Bankshares Incorporated, Richmond, Virginia, has been authorized to form an Edge Corporation, United Virginia Bank International, to be headquartered in Norfolk, Virginia. Board of Governors of the Federal Reserve System H.2, 1968-No.2, page 2.

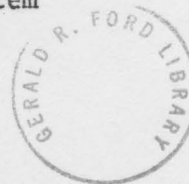


In 1962 Western Bancorporation established the first Corporation to be a subsidiary of a Bank Holding Company, Western Bancorporation International Bank. The company actually would have preferred having the Corporation a subsidiary of United California Bank, the company's lead bank, but the Board of Governors interpreted the restrictions of the Bank Holding Company Act as prohibiting such an ownership by a subsidiary bank. In actual fact the Corporation's operations were coordinated with those of the international department of United California Bank, although it also worked with at least two of the company's other banks. However, when the Board of Governors reversed its interpretation of the statutory restrictions in 1966, the Corporation's stock was transferred to United California Bank, and the Corporation's name was changed to United California Bank International.

In 1963 wholly-owned Corporations were formed by each, Marine Midland Corporation of Buffalo, New York, and Northwest Bancorporation of Minneapolis, Minnesota. The Marine Midland International Corporation works closely with the international department of the Marine Midland Grace Trust Company of New York, but also serves other banks in the holding company system. In contrast Northwest International Bank is somewhat more independent, although working primarily with its parent's lead bank, as few others in the holding company system are of sufficient size to have much international business.

Agreement versus Edge Corporation

The utilization of one versus the other of these types of Corporations has undergone drastic changes. Prior to 1930, 15 of the 18 Corporations coming under the jurisdiction of the Board were Agree-



ment Corporations. Between 1930 and the end of 1954 two out of the 4 new Corporations operated under an agreement with the Board. However, since 1954 only 5 of the 54 Corporations organized have been Agreement Corporations and 3 Agreement Corporations have converted to Edge Corporations. Today, of the 52 operating Corporations only 5 are Agreement Corporations: International Banking Corporation (owned by First National City Bank, New York), which was chartered in 1901 and was one of the first Corporations to sign an agreement with the Board of Governors; Bankers Company of New York (owned by Bankers Trust Company, New York), which was organized in 1931 and signed an agreement with the Board in 1938; and 3 that came under the jurisdiction of the Board subsequent to 1954, The Gallatin Co., Inc. (owned by Manufacturer Hanover Trust Company, New York), Virgin Islands National Bank (owned by First Pennsylvania Banking and Trust Company, Philadelphia), and First Foreign Investment Corporation (owned by The First National Bank of Miami, Miami, Florida).

Today, both types of Corporations are subject to the same supervision and virtually the same regulations, with the scope of activities of an Agreement Corporation being somewhat more restrictive. Because of this there are now only two basic reasons for choosing an Agreement rather than an Edge Corporation, both being of a technical or legal nature. One is where State banking laws have provisions for State banks to acquire the stock of a State-chartered international banking company, but not that of an Edge Corporation. Until recently this was true in California. The other reason for choosing an Agreement Corporation is where the purpose of the Corporation does not require



a capital of \$2,000,000, which is the required minimum for an Edge Corporation. This latter is illustrated by Bankers Company of New York, The Gallatin Co., Inc., and First Foreign Investment Corporation, each of which was utilized to acquire and hold a single stock issue. Of course, in a case where an Agreement Corporation has been in existence for a considerable period of time, as is true with International Banking Corporation, there may be a desire to maintain this continuity.

Additionally, there was another unique situation where the utilization of the Agreement Corporation made possible a stock acquisition by a member bank which could not otherwise have been done directly. Thus, First Pennsylvania Banking and Trust Company acquired the controlling stock of Virgin Islands National Bank since the latter signed an agreement with the Board of Governors and otherwise comes within the requirements of an Agreement Corporation under Section 25. Today, such a direct acquisition by a member bank can be made under the 1966 amendment to Section 25 and the March 1967 Revision of Regulation M.

"Twin" and Multiple Corporations

"Twin" Corporations developed from the differentiation between "Banking" and "Financing" Corporations in the 1957 Revision of Regulation K. Only the former could conduct an international business or hold stock of foreign banks, while only the latter could hold the stock of non-banking companies, issue debentures, or undertake underwriting operations abroad. This differentiation was based on the same philosophical concepts that were the foundation of the banking



statutes of the 1930's, which required the separation of commercial and investment banking. As a practical matter, this provision of the Regulation meant that even those banks that only desired to utilize a Corporation for holding stock in foreign banks and foreign finance companies were still required to have 2 Corporations, one of each type. As a result, during the period that this Revision was in effect, no fewer than 11 banks acquired "twin" Corporations. In 4 instances the bank acquired an additional Corporation so as to have twins,²⁴ and in the other 7, 2 new Corporations were chartered, although in one case one of the "twins," has never been utilized and is not yet opened for business.²⁵

The 1963 Revision of Regulation K abolished the major distinctions between these 2 types of Corporations, and as a result there is no longer any statutory or regulatory reason for a bank having separate "Banking" and "Financing" Corporations. However, of the 11 banks which had created "twins," only Bankers Trust Company has merged its Corporations.

The reasons for the banks' continuing to maintain "twin" Corporations do not appear to form any consistent pattern. While the philosophical concepts, which formed the basis for the original regulatory

²⁴First National City Bank retained its Agreement Corporation, International Banking Corporation, as its "Banking" Corporation and established a new Edge "Financing" Corporation. In 1957 The First National Bank of Boston converted its State-chartered Agreement Corporation into an Edge Corporation, but this is not considered as a new Corporation in this regard.

²⁵Irving International Banking Corporation.



distinction, seem to play a continuing role in the banks' thinking, the predominant reasons seem to be based more on various practical or administrative considerations. This appears to be particularly true where one or both of the Corporations have developed a particular role or character, such as establishing a New York presence for the parent, acting as a part of the foreign branch system in holding the stock of subsidiary foreign banks, or in specializing in project financing or underwriting. Also in some cases there may have been tax considerations which militated against a merger.

Six banks have multiple Corporations, other than those that were originally "twins." In all of the cases one Corporation has a special role or characteristic. Three cases arose prior to the 1963 Revision and occurred where an Agreement Corporation was acquired for a special purpose: to hold the stock of an English fiduciary in two instances, and to conduct a local banking business in the Virgin Islands in the other--and the parent bank subsequently organized another Corporation, or even "twins," to work more directly with its International Banking Department. The other three cases are within the past year, when banks with one or more Corporations headquartered with their International Banking Department, decided that they also desired to establish an international presence elsewhere through a Corporation's engaging in banking. In two instances the new Corporation was established in New York and in the other it was located in San Francisco.





Independent versus Integrated Corporations

Some Corporations operate with a reasonably high degree of independence from the parent bank's International Banking Department. Others have their operations and activities so closely integrated with the parent's International Banking Department that they are nothing but a corporate shell with no personality or character of their own.

As a general rule, the Corporations that are engaged in international banking in a city other than that of their parent bank, have developed a considerable amount of independence. This appears to be a natural outgrowth of the distances, communication problems, and time factors involved. On the other hand, the necessary coordination of the parent bank's overall international activities forms a natural barrier or limitation to the degree of such independence.

Corporations headquartered with their parent bank have not usually developed any appreciable amount of independence or character of their own. Of the 37 such Corporations in operation, only 2 or 3 have a completely independent staff and a clearly defined sphere of activities which is separate from the bank's International Banking Department. At most, only about 5 or 6 others show some lesser degree of independence. This is not particularly surprising when one considers that the primary purpose for most of these Corporations is that of a simple holding device for foreign stocks. Except for International Bank of Commerce, Seattle, which conducts a banking business at its Hong Kong branches, none of these Corporations is engaged in banking, which is only natural since they are located with the parent's International Banking Division. Furthermore, only a relative few make any loans

other than in the temporary employment of funds. Where a Corporation's function is so limited it seldom requires a large or independent staff, and this has the tendency of making it dependent on the staff of the International Banking Department.

Various Operations of the Corporations

The growth in the number of Corporations and of their parent banks has been accompanied by a marked expansion in the variety of operations which the Corporations have undertaken. By the mid-1950's the six Corporations then in existence really undertook only four types of operations. The first was the establishment of a New York presence and maintenance of a regular foreign banking business in that city; second, the maintenance of foreign branches; third, the establishment of subsidiaries operating in connection with foreign branches of the parent bank, primarily fiduciary companies and real estate holding companies; and, fourth, the holding of minority equity interests in foreign financing companies and in one instance in a foreign bank. The last two types of operations were, of course, attained through the exercise of the Corporations' power to hold stock in other companies. Of the six Corporations, three undertook only one of the above operations, two had both types of stockholdings, and one fulfilled three functions.

In the past 12 years, the operations that the Corporations undertook for their parent banks have had a prolific growth. While some completely new types of operations have appeared, many have resulted from the development and subdivision of the earlier operations mentioned above, this latter being particularly true in relation to the utilization of the stockholding power of the Corporations.



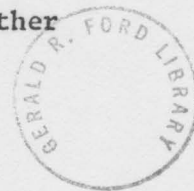
The establishment of an out-of-State presence is no longer limited to New York, for within the past year a New York bank, First National City Bank, has established a Corporation in San Francisco. Additionally, most Corporations, even though not "engaged in banking," now undertake some type of foreign financing, at least to the extent of acquiring bankers acceptances. (usually their parent's) or short-term foreign paper as a temporary means of employing unallocated funds. Furthermore, others have specialized in making medium-and long-term loans that are generally not made by their parent's International Banking Department, and a few have undertaken special project financing.

The foreign or overseas branch operations of the Corporations have diminished in importance insofar as volume is concerned, but have increased in diversity. A decade ago all foreign branch operations were fairly substantial in size, and similar in their scope of services to the foreign branches of U. S. banks in general. Today only the Hong Kong branches of International Bank of Commerce approach this type of operation, although they cannot yet be called substantial. However, there is a new variation in that the London office of Philadelphia International Investment Corporation is limiting its deposit function to Euro-currency time deposits. Additionally, First Pennsylvania Banking and Trust Company's Agreement Corporation, Virgin Islands National Bank, runs what amounts to a purely local banking business in that possession of the United States, even though two of its branches are situated in the adjacent British Virgin Islands.

The utilization of the Corporations' stockholding powers has shown the greatest amount of growth and variation. Assistance to the parent bank's foreign branches through stockholdings now takes not only the



form of wholly-owned fiduciaries and real estate holding companies, but also nominee companies, controlling or minority interest in various types of finance companies, and minority interests in government-sponsored development finance companies. This last is often considered a political or public relations necessity for the local branch. An entirely new function has appeared in the form of subsidiary banks in lieu of foreign branches. These have occurred where foreign branches were not permitted under local law, or because, in a given situation, other considerations led the parent to choose the affiliate route rather than direct branching. Equity interests in finance companies--other than those cooperating with local foreign branches--have become of vastly greater importance, and now include controlling as well as minority interests. Some are even considered as substitutes--though admittedly second choice--for branches or subsidiary banks where these are not permitted. Minority interests in foreign banks have not only increased tremendously, but have often developed into a method of further cementing correspondent relationships. Another new development has been the creation of the foreign-based "alter ego" subsidiary, which exercises basically the same powers as the Corporation itself. These have been formed for various reasons, including among others tax considerations, the compartmentalization of operations in certain geographic areas, and the avoidance of direct involvement of the parent bank's name in certain operations. More recently equity investments have been utilized in establishing "joint ventures" with one or more partners, which may or may not include other Corporations. Another



innovation has been the formation of companies to tap the Euro-dollar bond market. These have become increasingly important with the tightening of the Board's voluntary foreign credit restraint effort. Some of these companies have taken the form of an "alter ego" company, while others have been in the form of a "joint venture."

The variety of possible combinations of the operations for which the Corporations have been utilized by their parent banks is apparent. It also appears equally obvious that a really broad utilization of these various operations requires time to develop. In actual practice, less than half of the 37 parent banks are currently utilizing their Corporations in more than 3 of the ways set forth, and of these only 1 acquired its first Corporation subsequent to 1963. In contrast, of the parents using their Corporations for less than 4 of these operations, only 5 established their first Corporation in 1963 and all the others are of more recent origin.

Despite the variety of the current operations of the Corporations as set forth above, they fall into four groups, or basic functions, namely:

- (1) Foreign banking operations in the United States;
- (2) Direct overseas operations;
- (3) Specialized financing, including underwriting; and
- (4) Equity investments.

Some of these functions, while easily distinguishable, have certain common features. For example, the first two categories ordinarily require the Corporation to be, or anticipate being, "engaged in banking," whereas the others need not; and a foreign presence may be established by direct branching or through a subsidiary. Furthermore, some



functions can be combined in a single Corporation more easily than others. Thus, Corporations utilizing any of the other three functions may also have stockholdings, but it is unlikely that those "engaged in banking" would also engage in specialized financing to any considerable extent.

In the following two chapters, these basic functions are discussed as to their development, the extent of their utilization and the rate of their growth over the past 12 years. Also past and developing trends are investigated and future possibilities explored.



CHAPTER V

THE BASIC FUNCTIONS OF A BANKING NATURE

As noted in the preceding chapter, the operations of the Corporations encompass four basic functions. Three of these are entirely or principally of a nature that is commonly related to banking in the United States. These form the subject matter of this chapter. The fourth function, the acquisition and holding of equity interests, is generally prohibited, except in strictly circumscribed circumstances, to U. S. banks. It is also the function which has shown the most attraction for the international banking community in this country. This attraction has resulted in its having the most phenomenally large and varied growth of any of the basic functions of the Corporations. Because of the many facets involved in its increased utilization, it is treated separately in the following chapter.

Direct overseas operations and specialized financing each have a distinct role in the current operations of the Corporations. However, among the Corporations' banking type operations it is the full fledged international banking business which has been the center of interest and hence the principal focus of growth among these activities.

International Banking Operations in the United States

Not since Colonial times, or at the latest the first years of the Republic, has New York been challenged as either the national or international financial center of the United States. Beginning with the



period of World War I it also became one of the principal financial centers of the world and eventually one of the world's two financial capitals. As a result, few foreign businessmen or financiers that visit the United States do not at least pass through New York City. There is hardly a major American business that does not maintain some sort of office in New York, and a large number of those with overseas branches or operations have their International Corporation or Division headquartered there. Because of this there is no other place in the country, if not in the world, where information on the current international conditions, trends, and even rumors is so readily available.

New York thus offers the maximum exposure to possibilities in international financial transactions and the most comprehensive information on international conditions. Logically, it is also the location of the vast majority of foreigners' deposits in the United States. Under these circumstances it is not surprising that the non-New York banks, which have been most aggressive in the field of international finance, have seen distinct advantages in being able to establish a New York presence. Even somewhat less aggressive banks have also found such a presence a necessity. A necessity, that is, if they are to remain the principal banker for some of their important local customers, many of whom in recent years have entered into international operations, or upgraded such activities. Besides these local situations, there are also the competitive forces at play among the larger banks throughout the country, each trying to maintain its share of the national and international business of the principal U. S. companies. These companies have operations that are spread throughout this country and much of the rest of the world, and their financial requirements exceed





the capabilities of any single bank. To maintain a share of this business, whether of local or national companies, banks have found that they must be in a position to extend a broad range of services. On the foreign side many of these services must be available in U. S. cities other than where the bank's head office is located, primarily in New York.

The use of domestic correspondent banks in such cases has often proven more futile than useful. This is true, because any correspondent with adequate international services is no doubt also a competitor, not only for any international business, but also for a more lucrative share of the national business of the large companies. As compared to correspondents, a subsidiary Corporation offers the banks an opportunity for a direct representation in another State. Of course, the business in the United States of these Corporations is limited by statute to that which is incidental to their international business. However, this does not inhibit certain deposit and loan relationships and it has not prevented the Corporations from being an effective device for the banks in establishing their presence in international financial centers outside their own State.

The local competitive realities have at times been highlighted by the near coincidental establishment or transfer of some of the Corporations. Thus in 1962 the two largest banks in Chicago each established a Corporation in New York to undertake an international banking operation. Eighteen years after Bank of America, New York, opened, and five years after the establishment in that city of what is now United California Bank International, there suddenly appeared in a single

year three Corporations in New York owned by California banks. Even more enlightening as to the strength of these competitive factors is the fact that in the past year a New York City bank, First National City Bank, has felt it desirable to establish a banking Corporation in San Francisco, a reversal of what had been the common pattern.

Growth of Banking Operations in the United States

The first, and for 30 years, the only such operation in New York by a wholly-owned subsidiary was that of The First National Bank of Boston. In 1918 it established an Agreement Corporation with its operating office in New York. In 1957 it was converted into an Edge Corporation, now Bank of Boston International. In 1949 Bank of America National Trust and Savings Association, San Francisco, established a New York-based Corporation, Bank of America, which since then has been the largest and most active of all Corporations with banking operations. It was not until 1962, thirteen years later, that another Corporation was organized to undertake similar banking operations. Since then there has been a rapidly increasing interest in this type of operation and today there are 13 Corporations operating an international banking business in New York and another owned by a New York City bank is located in San Francisco.

The table on the following page shows the growing breadth of participation in this type of operation, the relative newness of most of the entries, and that the banks undertaking this type of operation have generally been among the larger of the non-Metropolitan New York banks.



TABLE 3

BANKING CORPORATIONS AND THEIR PARENTS

<u>Date</u> <u>Estab-</u> <u>lished</u> ^a	<u>Parent Bank</u> <u>Corporation</u> (current name)	<u>Parent's</u> <u>Rank</u> ^b
1918	The First National Bank of Boston Bank of Boston International, New York	10
1949	Bank of America NT&SA, San Francisco Bank of America, New York	1
1962	Continental Illinois Nat'l Bank & Trust Co. of Chicago Continental Bank International, New York	2
1962	The First National Bank of Chicago First Chicago Int'l Banking Corp., New York	4
1962	United California Bank, Los Angeles United California International Bank, New York	7
1963	Northwest Bancorporation, Minneapolis Northwest International Bank, New York	52 ^c
1965	State Street Bank and Trust Company, Boston State Street Bank Boston International, New York	41
1966	Bank of California National Association, San Francisco Bank of California International, New York	19
1966	Mellon Nat'l Bank and Trust Company, Pittsburgh Mellon Bank International, New York	8
1967	Crocker-Citizens National Bank, San Francisco Crocker-Citizens International Bank, New York	6
1967	Philadelphia National Bank Philadelphia International Bank, New York	17
1967	Wells Fargo Bank, San Francisco Wells Fargo Bank International Corp., New York	5
1967	First National City Bank, New York First National City Bank (International), San Francisco	2
1967	Northern Trust Company, Chicago ^d Northern Trust International Corporation	29

^aWhere a Corporation was established and subsequently transferred so as to undertake a banking operation, the later date is given. Where a Corporation converted from an Agreement to an Edge Corporation, but continued to be engaged in banking the earlier date is shown.

^bIn order of December 31, 1967, deposits of non-Metropolitan New York banks, except for First National City Bank which is ranked among New York City banks only.

^cRanking is of the lead bank, Northwest National Bank, Minneapolis.

^dNot yet opened for business as of December 31, 1967.



This list also shows that in less than six years the number of cities with banking institutions maintaining a subsidiary banking operation in New York has jumped from two to seven, and additionally one New York bank now has such an operation on the Pacific Coast. Not only has the number of these Corporations increased, but their total assets and total capital accounts have grown at an even faster rate. While the increase in numbers was six-fold, that in both of these accounts was more than eight-fold, so that by mid-1967 they were \$1,267 million and \$127 million, respectively. Despite the increasing number of Corporations, Bank of America has maintained its position as the predominant factor, so that in mid-1967 it still had well over half the total assets and almost half of the total capital accounts.

Coordination of Operations with those of the Parent

As noted earlier, all of the Corporations conducting international banking operations tend to have some degree of independence, but such independence is limited by the need for an over-all coordination of the bank's international operations. The manner of attaining this coordination varies from one institution to another and, as a result, there are variations between the Corporations both as to the amount of independence and the manner of operating.

Primarily two factors appear to determine the form of this coordination and, hence, the degree of the Corporation's independence and the scope of its operations. These are the geographic or time zone difference between a Corporation and its parent, and the role that the parent visualizes for the Corporation. While the former unquestionably exerts an influence on the latter, each can have a separate effect on the manner of coordination finally chosen.



The greater the geographic distance, the greater the tendency toward more independence. This can be seen in any branch banking operation, especially among foreign branches. The increased cost of communication is an example of the forces which militate for this greater independence. Furthermore, where the distance is such that different time zones are involved, certain integrated types of operations become less practicable, if not impossible, and hence operations of a more independent character become more likely.

Different banks can conceive of a variety of different roles for a Corporation located in another State. They may see it purely as an extension of the international banking department's loan platform, tellers' cages, etc.; as a specialized separate department with limited functions; like a domestic branch with limited independence; similar to a foreign branch with even less restrictions on its independence; as an independent entity with coordination only at the policy level; or as the center of certain of the bank's international operations. Furthermore, the parent may visualize the Corporation fulfilling one role in relation to certain functions and yet another role as to other functions. Thus in its credit operations it may be closely tied to the parent's International Banking Department, but in foreign exchange transactions it may be the center of all such operations for the bank.

In actual practice there are no two Corporations that maintain exactly the same relationship with their parent. However, the Corporations do seem to fall into two general groups. The first act as out-



of-State extensions of the parent's international banking department. These may also have independent operations such as maintaining deposit accounts, making loans and performing other services, but the bulk of the transactions handled are for the account of the parent bank. Experience to date indicates that in these cases the parent and the Corporation are usually in the same time zone. The second general group operates more like independent entities. These Corporations often develop substantial customer relationships, deposit and loan, which have no direct connection with the parent bank, although they naturally also serve the parent's customers. These Corporations may also become chiefly responsible for certain of the parent's international functions such as foreign exchange trading. Thus far these Corporations have tended to be in a different time zone from their parent, and to have a greater degree of independence than the Corporations in the first group.

In all cases the directors, and often the principal officers, of the Corporation include the top executive officers of the parent bank. Thus at the top policy level there is complete coordination. The degree of coordination and cooperation at the lower levels seems to depend on the role of the Corporation and on the individuals concerned. Where the role envisages only a minimum of independence, major decisions are made at the international banking department and, hence, coordination is achieved automatically. On the other hand, where there is considerable independence, coordination may be achieved



through the executive officer of the Corporation, or may be diffused through the organization, i.e., the various area loan officers, credit review officers, etc. The degree of such diffusion appears to depend largely on the individuals involved and the size of the operation.

Types of Operations Undertaken and Service Offered.

As of mid-1967, all 11 of the Corporations with international banking operations in New York were maintaining a deposit and loan business, and 10 of the 11 also had customer acceptance finance outstanding. However, only 7 had sufficient demand deposits and acceptances outstanding so as to appear to be technically "engaged in banking" under Regulation K²⁶. Two of these only opened in New York in 1966 or 1967 and the others in 1962 or earlier. On the other hand, only 1 of the 4 not technically "engaged in banking" opened prior to 1965. Furthermore, only 6 of the 11 Corporations appeared in mid-1967 to be funding their loan operation through deposits received, and for these the loan-to-deposit ratio varied widely. Here again, the period of time the Corporation has been operating a banking business does not always seem to be the controlling factor, as one of the 6 funding their loan operations with deposits only started such operations in 1966, while 2 that are not so funding their loans commenced operations four or five years ago.

²⁶Section 211.2(d)--A Corporation is "engaged in banking" whenever it has aggregate demand deposits and acceptance liabilities exceeding its capital and surplus. Regulation K, page 2. However, the Board has issued an interpretation that deductions permitted in calculating required reserves may also be deducted in calculating "aggregate demand deposits" under this section. Interpretations of the Board of Governors of the Federal Reserve System, June 1967, ¶5705, page 481.



The above data indicate that while all of these Corporations basically offer checking account, loan, and acceptance services, the emphasis and manner of operating vary considerably. This becomes even more noticeable when one studies the Corporations! other typically internationally oriented operations such as foreign exchange, letters of credit, and collections. Perhaps one should also include with this second group of services those which the Corporation offers purely as an agent of the parent. A general insight into the operations of the Corporations and their variations are best understood through specific examples.

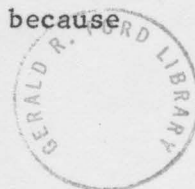
Bank of America is without doubt not only the largest, but also has the greatest scope of operations of any of the Corporations. It has the broadest base of deposits, which is not surprising when one realizes that it has been active in this area more than three times as long as any other of these Corporations, except Bank of Boston International. Additionally, it has the advantage of being a subsidiary of the world's largest bank and one that, except for a single New York bank, has more overseas branches than any other United States bank. With this deposit base and its parent's contacts it has been able to aggressively enter the New York international financial market and to become a not inconsiderable factor in that market.

To lure new borrowing clients, either in making their first international banking account or in transferring their foreign business from previously established bank connections in New York, Bank of America has as broad a range of financing methods as virtually any New York institution. Besides the usual short-term commercial loan, advances on

collections, acceptances, and letters of credit, it also makes term loans and issues deferred payment letters of credit. Lines of credit to foreign correspondent banks and to large international concerns are often available at the Corporation in New York, as well as in San Francisco with its parent. Any exceptionally large credits may, of course, be partially participated to its parent, although the Corporation alone has a single borrower limit of over \$4.5 million.

Besides these more or less standard services, it can also offer a large range of other international services, both on its own and drawing on the knowledge and abilities of its parent's California offices or those in foreign countries. It has established itself as an important factor in the New York foreign exchange market, operating primarily on its own, but at times as agent for its parent.

These foreign exchange operations, both in the spot and future markets, have an important influence on the balance sheet, not only of Bank of America, but of all other Corporations handling a volume of such transactions. According to the custom of the New York market, foreign exchange transactions, and all other international payments, are payable in Clearing House Funds unless Federal Reserve Funds are specified. While Federal Funds are payable the same day, Clearing House Funds are not payable until the following business day. This means that in liquidating most foreign exchange transactions or other payments of funds, the amounts will appear overnight in both the "Due from Banks" and the "Deposits-Officers Checks outstanding" accounts. This is, of course, also true for all New York City banks, but because



of their relatively larger deposit bases, the effect of this "float" on their balance sheet is largely masked. However, for the Corporation handling a large volume of these transactions, such as Bank of America, the "Due from Banks" account often reflects a very high amount in relation to Total Deposits. While this type of transaction was certainly not the only reason, it is interesting to note the apparently highly liquid positions of the Corporations with banking operations in New York. As of mid 1967, only 2 of the 11 such Corporations showed "Cash Assets" of appreciably less than 50 per cent of deposits.

In contrast to Bank of America, Bank of Boston International over the years has acted principally as an agent for its parent bank, rather than as a separate entity. Checks drawn in international transactions on accounts at the parent in Boston are honored at the Corporation. Similarly foreign loan funds can be disbursed or payments made through the Corporation, and documentary credits can be honored and processed at the Corporation. There is never any question of establishing contact during banking hours when there are problems to be answered or important policy decisions to be made, as both offices are in the same time zone. Thus, where the bulk of the operations of Bank of America are for its own account, a large proportion of the transactions at Bank of Boston International have been for the account of its parent in Boston. Of course, on the other side of the ledger the latter had almost at its fingertips all of the expertise of the entire International Banking Department of its parent. The fact that it has acted principally as an agent for its parent, does not mean that Bank of Boston International has not maintained certain services of its own. On the contrary it has



maintained checking accounts and made loans on its own, although it apparently has not done any extensive acceptance financing in its own name, and foreign exchange operations are still handled primarily in Boston.

Another variation in the parent's utilization of a New York banking Corporation is illustrated by Continental Bank International. The Corporation in New York does virtually all of the foreign exchange trading for its parent bank, as well as for itself. As might be expected its "Cash Assets" form a relatively larger proportion of Deposits than is true of most of these Corporations. In addition to this special operation, the Corporation also maintains checking accounts, makes loans, and offers the services of a full fledged international operation, and in general competes actively for international business in the New York market.

Summary

The number of banking institutions which have utilized a Corporation to establish an international "out-of-State" presence has grown six-fold over the past 12 years, and now encompasses a far broader geographic spread. However, as in 1954, only about one-third of all the banks with Corporations are utilizing them in this manner.

There is considerable variation in the manner in which the international operations of the parent banks and of the Corporations are coordinated and this naturally influences the degree of independence the Corporation may have. Distances, time zones, and the differing roles visualized for the Corporation all enter into these variations. It also affects the emphasis the Corporation may place on different services and operations.



In general, all the Corporations tend to offer, directly or indirectly, the same scope and types of international financial services as are offered by their parent banks and by the other commercial banks with which they compete for foreign-oriented customers.

Direct Overseas Operations

In 1916 the passage of Section 25 of the Federal Reserve Act first permitted national banks to acquire the stock of "Agreement" Corporations, and in 1919 Section 25(a) was enacted making possible the Federally chartered "Edge" Corporations. Shortly after the enactment of the former legislation The National City Bank of New York (now First National City Bank) acquired the controlling interest of International Banking Corporation and it became an Agreement Corporation. This company was established in 1901 and at the time it entered into an agreement with the Board of Governors was already operating a number of foreign branches scattered through various parts of the world. In the next few years other Corporations were organized and also established foreign branches.

Until 1925 the Corporations actually operated more overseas branches than did the banks themselves.²⁷ Then there began a period of two decades during which many foreign branches were closed and only a few new ones were opened. At the same time most of the branches of the Corporations were transferred to banks, usually the parent, but in one instance to a foreign bank, The Royal Bank of Canada.

²⁷ "United States Banking Organization Abroad," Federal Reserve Bulletin, December 1956, page 1289.



By the middle of the 1950's, Corporations were operating only two active branches, the Paris Branch of Morgan & Cie. Incorporated, and Bank of America's branch in Dusseldorf, Germany. Additionally there were, and still are, two inactive offices, Chase International Investment Corporation's Paris Office and International Banking Corporation's London Office, both of which had transferred their banking business to their parent banks, but continue to maintain a legal presence for technical reasons.

Within the next nine years the Paris Branch of Morgan & Cie. Incorporated was combined with that of Guaranty Trust Company, when the two parents merged, and the branches of Bank of America were transferred to its parent bank. By the time of the transfer to its parent, Bank of America had a branch in each Dusseldorf, Paris, Beirut, Singapore, Kuala Lumpur, and Hong Kong, and two in Guatemala.

During the 1960's three new direct overseas operations have been undertaken through the use of Corporations. All are distinct from the previous types of overseas operations of the Corporations.

In 1964 the International Bank of Commerce, which had been formed in 1963 by The National Bank of Commerce of Seattle, opened a branch in Hong Kong. Since then four additional branches have been opened in that Crown Colony. When these branches opened the parent bank had no overseas offices of its own. These branches are not as yet strongly engaged in financing international trade, but concentrate more on loans to local businesses and individuals. However, they do establish a Far East presence for their parent bank, whose international transactions are largely oriented toward that area. The opening of the parent bank's London branch will no doubt assist these Asian operations.





Early in 1967 Philadelphia International Investment Corporation opened an office in London. Such an office must be considered a substitute for the establishment of a direct branch by The Philadelphia National Bank. Its purpose would seem to be the tapping of the Euro-dollar market to assist the parent bank in financing the foreign needs of its customers without affecting its position under the voluntary foreign credit restraint program. It will also give the parent organization a European presence and the ability to maintain a closer contact with the financial developments in that area.

The unique position of the Virgin Islands National Bank calls for some special comments. In 1960 it signed an agreement with the Board and its controlling stock was acquired by The First Pennsylvania Bank and Trust Company, Philadelphia, a State-member bank in the Third Federal Reserve District. Part of its uniqueness is that, although it fits precisely into the requirements of the Act, it was probably not a situation originally contemplated by the drafters of the legislation. While it operates under an agreement with the Board, it was chartered by and also remains subject to the jurisdiction of the Comptroller of the Currency. Subsequent to its agreement, the bank opened two branches in the adjoining British Virgin Islands, and thus technically is operating foreign branches. It is thus the only Corporation situated outside the United States proper, the only one under the direct jurisdiction of both the Board and the Comptroller, and one of the few with overseas branches. However, its operations are not such as are generally considered as having a basic international character. It conducts a general local banking business within the archipelago, is not particularly

concerned with the financing of foreign trade, and treats all branches as local, whether in the American or British Virgin Islands, except insofar as different treatment is required by law.

Summary. The direct overseas operations of the Corporations was of considerable importance in the earliest stages of their development. Today, however, these operations play a relatively small part in the activities of the Corporations as a whole. In the past few years there has been some indication that there may be some renewal of interest in direct overseas activities, as shown by the establishment of branches in Hong Kong and a limited purpose London office, but this current interest seems to be in activities of a far more restricted character or different scope than was true in the early periods.

Specialized Financing

Some of the Corporations that are located with their parent and not "engaged in banking," have undertaken specialized financing, usually in conjunction with other functions. This financing has taken a number of different forms, ranging from relatively simple term loans to the more sophisticated formation of syndicates which undertake loan-equity packages for more complicated projects.

One type of operation which falls perhaps marginally within this function of specialized financing and deserves mention, is the participations with the International Finance Corporation ("IFC"). Over the years IFC has put together a number of loan-equity packages to assist in the financing of various private and government-sponsored organizations in the developing countries. Some of these have been producers or manufacturers, while others have been development finance companies, which are to assist local producers and manufacturers. A number of the



Corporations have taken a percentage of one or more of these packages in participation with IFC, and some have turned out to be very profitable where the stock has gone up sharply in value. Since virtually none of the expertise that goes into the arrangement of the financing is contributed by these Corporations, such participations can hardly be considered as one of the more sophisticated forms of specialized financing by the Corporations. In many ways such participations are similar to the acquisition of foreign paper through brokers, as in neither operation are the results due to the prior development of a foreign clientele, foreign contacts, or any special expertise in international financial operations.

The simplest form of specialized financing by the Corporations is where the parent's International Banking Department does not choose to make certain types of loans--for example, term loans--and the Corporation has become the arm of the bank which specializes in these types of international financing. Some of these arrangements were consciously planned, while others developed more or less unconsciously as the customary term of foreign loans lengthened. Usually the Corporations fulfilling this particular function also have other activities, although thus far they have not usually included those which would cause them to become "engaged in banking."

Other Corporations have undertaken to give extensive assistance to customers in establishing overseas operations. This has often included market surveys and extensive investigations of the availability of local financing and local equity partners. One or two of the Corporations have at this point turned over the financing to foreign branches of the parent bank. Others have continued on and either undertaken the financing



themselves or organized syndicates to underwrite the enterprise. Some of these arrangements have been extremely complicated, including the finding of local or foreign partners, arranging for the assistance of companies with specialized skills or knowledge, the placing of bonds or debentures, arranging term loan facilities and short-term operating lines of credit in foreign or local currencies, and the public sale of equity interests. Only a very few Corporations have undertaken the more sophisticated of these operations.

Underwriting has also been done by a few Corporations. This usually has taken the form of debt obligations and in some instances they have been a means of obtaining contacts and at the same time adding to the Corporation's security or loan portfolio, by taking their portion of the issue and not reselling it. There have been only a few known instances of the underwriting of stocks. One Corporation has on several occasions requested the Board's consent to participate in a syndicate underwriting a Mexican stock, and in another instance took a portion of an underwriting in conjunction with a foreign subsidiary.



CHAPTER VI

EQUITY INVESTMENTS

No change in the utilization of Corporations has been as dramatic as the growth in the use of their powers to make equity investments in foreign companies.²⁸ In the mid-1950's the Corporations had a total of eight stock holdings at a cost of \$2 million whereas by mid-1967 they had 327 holdings which cost \$219 million. As striking as these figures are, they fail to illustrate the changing and increasing multiplicity of purposes of such equity investments.

Of the eight holdings in 1954, there was one small minority investment in a foreign bank, a similar minority investment in a foreign finance company, one holding in a New York discount house and the remaining stocks were all in companies servicing the parent's foreign branches. Today over 60 per cent of the dollar value of investments is in foreign banking institutions. These investments are primarily utilized as an alternative to direct foreign branching or as a means of strengthening correspondent bank relationships. Only a relatively small amount is in the stock of companies servicing the parent's foreign branches. Various types of finance and investment companies, including development finance companies, constitute the bulk of the remaining investments. Although a

²⁸ "Foreign companies" as used here includes domestically-chartered organizations in which investments are permitted by statute. The statistical basis is set forth in Appendix 3.



minority of the dollar value, they represent almost two-thirds of the number of individual stock holdings. This type of investment is sometimes used in conjunction with foreign branch networks or as a source of local funds. In other instances it is regarded as a means of broadening and improving contacts with correspondent banks and commercial enterprises, and as a source of financial information and servicing. In terms of dollars, there has been only a relatively small investment in nonfinancial companies and such holdings have usually been acquired in connection with an extension of credit, the majority in participation with the International Finance Corporation.

The table on the following page shows the general growth, and to some degree the changing utilization of this power of the Corporations to hold the stock of foreign companies. To attain a real understanding of the variety of ways in which this stockholding power has been utilized, each of the classes of investment must be scrutinized. The following sections undertake to do this both by breaking them down into further subtypes and by analyzing the various functions which the similar or different investments may fulfill. However, before approaching the various functions of these investments, it is of interest to see something of the changes in their geographic spread and their degree of control.

Geographic Distribution of Investments²⁹

At the end of 1954 the Corporations had eight stock investments, six in Europe and one each in Latin America and the United States. Today the

²⁹ Appendix 3 contains a table with this distribution. The geographical location of the companies is based on the site of their principal operations, not necessarily where they are chartered.



TABLE 4
EQUITY HOLDINGS OF THE CORPORATIONS

Year end ^a	Banking Institutions ^b		Finance Companies ^c		Nonfinancial Companies		Totals	
	Dollars	No.	Dollars	No.	Dollars	No.	Dollars	No.
1954	*	6	*	2	-	-	2,004	8
1955	*	7	*	5	-	-	3,956	12
1956	*	7	*	4	-	-	3,980	11
1957	*	9	*	5	-	-	16,002	14
1958	*	10	*	5	*	2	16,466	17
1959	*	13	5,580	7	*	3	20,479	23
1960	16,356	20	9,997	12	-	-	26,353	32
1961	18,533	27	9,848	18	106	2	28,487	47
1962	31,460	37	16,552	36	804	14	48,816	87
1963	44,932	46	22,969	79	1,091	18	68,992	143
1964	50,099	54	39,006	129	1,786	24	90,891	207
1965	91,924	70	50,776	159	3,614	31	146,314	260
1966	128,833	82	66,175	182	4,580	43	199,588	307
6/67	143,632	94	70,173	188	5,099	45	218,904	327

*Data deleted to preserve confidentiality.

^aAs of December 31, except 1967, as of June 30.

^bIncludes bank, bank holding companies, trust companies, nominee companies, and realty holding companies - bank premises.

^cIncludes development finance companies and finance and investment companies.

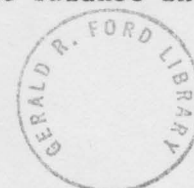
See Appendix 3 for the sources and bases of these statistics.



Corporations' more than 300 investments are in more than 60 countries located on 6 continents and in most of the major archipelagos. As of mid-1967 over one-third of investment cost was represented by holdings in Europe; almost one-fourth by holdings in Latin America, and approximately one-sixth in Africa, the conglomerate grouping of the Bahamas, Bermuda, and Canada. Each of these and the other areas have interesting characteristics, including when they were made and in what types of companies.

Europe was the major focus for foreign equity holdings in 1954 and it remains so today, but with a less predominant position. However, the types of investments have changed completely. Twelve years ago five holdings were in foreign branch related companies, i.e., trust companies or bank premises holding companies, and only one was in a bank. Of the \$78 million invested in 93 stockholdings in mid-1967, over two-thirds were in banks and bank holding companies, barely two per cent in branch related companies, with most of the balance being in finance and investment companies. Whereas the investments 12 years ago were in only three countries, they are now located in all of Western Europe except for Ireland, Denmark, Norway, Sweden and Portugal.

While the first investment in Africa was made in 1955, there were still only three at the close of the decade, all being wholly-owned subsidiary banks. Today there are investments in companies chartered by at least 17 African countries and several other holdings in banking organizations which operate in a number of the African countries. In mid-1967, there were 43 investments totaling \$37 million, of which almost \$35 million was in banks and bank holding companies and almost all of the balance in finance organizations.



Latin America attracted but one or two investments throughout the latter part of the 1950's, but in 1960 the number and amount began to increase, the latter exceeding \$1 million in that year. By June 1967 there were 87 investments costing over \$50 million. In contrast to Europe and Africa, the investments in Latin America were for several years much more closely balanced between banks and finance companies. However, beginning with 1965, the holdings of bank stocks have taken the lead and today amount to almost two-thirds of the total investment. While only a small amount-- about five per cent of the area total is invested in non-financial organizations, this represents almost half of all such equity holdings.

The developed areas of the Bahamas, Bermuda and Canada became an early focus for investments by the Corporations, primarily in wholly-owned subsidiaries. The investments have tended to be relatively few in number, but large in amount with the cost of the holdings in banks and finance companies having been fairly evenly balanced since 1965. In contrast to finance companies in other areas, virtually all of these have been in "alter ego" type operations and they have often specialized in financing trade and development in Latin American countries.

Investments in Asia and the Near East began in 1955 and have always been predominantly small minority holdings. Thus while the number of investments has been large, actually competing fairly closely with Latin America for second place after Europe, the amount has been small, representing less than five per cent of total investments in mid-1967. Well over 80 per cent of the total is invested in non-bank financial companies.

Australia and New Zealand represent the newest of the areas in which the Corporations have become interested. The investments here are still relatively small both in number and amount. There are no holdings of bank stock in this area.



Investments in the United States and its possessions have played only a very minor part in the Corporations' stock portfolios, with the exception of the last years of the 1950's when there was a sizable investment in a New York discount house which has been held for many years. Despite this minor role as to number and amount of investments, proposed stockholdings in such companies have often raised thorny questions of regulatory policy because of statutory limitations on such investments.

Degree of Control

Over the past 12 years there have been many changes in the degree of ownership represented by the Corporations' investments as between the virtually wholly-owned subsidiary (over 90 per cent) the controlled subsidiary (45 to 90 per cent) substantial minority interests (10 to 45 per cent) and small minority interests (10 per cent or less). Until 1960 the principal emphasis was on the wholly-owned subsidiaries, both as to amount invested and number of investments. The year 1961 saw the beginning of a transition with the total number of the two kinds of minority investments exceeding the number of wholly-owned investments although their dollar value remained less than one-seventh of total costs. In 1962 controlled subsidiaries appeared for the first time and holdings of wholly-owned subsidiaries represented a dwindling proportion of total dollar investments. This trend has continued to the present despite the increase in the number of such investments.

Large dollar investments in substantial minority interests began to appear in 1963 and have continued to show substantial growth in recent years. By mid-1965 the two types of minority investments represented over half of the Corporations' total stock portfolio. Measured by the dollars invested there seems to have been a generally increased emphasis on the



middle ground of the controlled subsidiary and the substantial minority interests, as distinguished from the extremes of the wholly-owned subsidiary and the small minority interest.

It is interesting to note the relationship between the degree of control and the average size of investments. From 1957 until 1962 the relationship was direct, the greater the control the greater the average investment. However, since the advent of controlled, but not wholly-owned, institutions, this type of holding has represented the largest average investment by a considerable margin.

There are also certain geographic concentrations relative to the degree of control. Of the virtually wholly-owned subsidiaries over nine-tenths of the dollars invested are in Europe and the Bahamas, Bermuda, and Canada group with most of the balance in Africa. Nearly nine-tenths of the amount invested in controlled subsidiaries is in Latin America and Europe. Over two-fifths of the dollar investment in substantial minorities is in Africa, over one-fourth in Latin America, and one-fifth in Europe. Europe and Latin America represent three-fourths of the dollars invested in small minority interests with over one-tenth in Asia and the Near East.

Investments in Banking Institutions

In the mid-1950's banks and bank-related companies were the predominant foreign stock investments of the Corporations. This remains true today, but the functions and purposes of such holdings have undergone considerable change and development. At the end of 1954 there was only one very small stockholding in a commercial bank, the bulk of the investments being in bank-related companies. Today the holdings in commercial banks, directly or through holding companies, represent two-thirds of all types

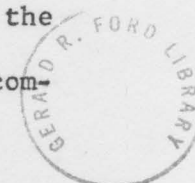


of investments, while bank-related companies are only slightly over five per cent of the total.

In 1954 investments in bank-related companies were limited to English fiduciaries, which were operated as adjuncts of the parent London branches, and branch premises holding companies. Today, investments in banking institutions include not only these, but also full-fledged trust companies, some with attributes approaching those of commercial banks, and nominee companies. Some of these operations are independent and others are related in varying degrees to the activities of an overseas branch of the parent bank. With the exception of some of the full-fledged trust companies, all are controlled, if not wholly-owned subsidiaries.

However, the change in the utilization of bank-related companies has been minimal compared with the expanded use of stockholdings in commercial banks and bank holding companies. In 1954 these investments represented only an exceedingly small part of the total holdings of \$2 million. Today, they constitute over two-thirds of the \$219 million in total stock investments. From a single minority holding in a small European bank they have expanded to include controlled banks in Africa, Latin America, Canada and Europe, plus several substantial interests in large regional banking systems, to say nothing of numerous smaller minority interests. Today, they function in lieu of branches for some institutions, for some they supplement branch operations, for others they are an alternative to establishing a foreign branch network, and yet for still others a method of strengthening relationships with foreign correspondents.

The function that an investment is to fulfill and the degree of control represented by that investment are usually interrelated, but this is not to say that a given function requires a single given degree of control, or



vice versa. Thus, an investment, made in lieu of foreign branches may achieve that end through either wholly-owned, majority controlled, or substantial minority interests. Despite this, the fulfillment of certain functions generally seems to tend toward investments within certain degrees of control. Thus, for purposes of analyzing the various investments in banks and the functions that they fulfill, they are discussed under the following subdivisions: holdings representing control; substantial minority holdings; and smaller minority holdings. Additionally, there are certain functions of a very specialized nature that deserve separate comment. Except where special reference is necessary, the following refers only to investments in commercial banks and bank holding companies, and does not include bank-related companies, whose functions are normally self-evident.

Holdings Representing Control³⁰

The first such acquisition was made by International Banking Corporation in 1955 with the purchase of control of Bank of Monrovia, Monrovia, Liberia. This was followed in 1957 by Bank of America's acquiring virtually all of the outstanding stock of Banca d'America e d'Italia, Milan, Italy, which had also been established by A. P. Giannini, founder of Bank of America NT&SA. In 1958 and 1959 International Banking Corporation and Chase Manhattan Overseas Banking Corporation each organized subsidiary banks in South Africa.

These last two subsidiaries have thus far been the only controlled subsidiary banks which have been newly established by a Corporation, all others having been acquired through the acquisition of stock of a going

³⁰ These include wholly-owned, with over 90 per cent, and controlled, with over 45 to 90 per cent.



concern, which at times has required the payment of a premium. They also illustrate one of the principal reasons for establishing such subsidiaries, as the Corporations' parent banks were not permitted by South African law to establish branches in that country.³¹

It was not until 1962 that a Corporation acquired a barely controlling interest in a foreign bank. In that year Chase Manhattan Overseas Banking Corporation acquired approximately one-half of the outstanding common stock of Banco Mercantil y Agricola, Caracas, Venezuela, and Banco Lar Brasileiro S. A., Rio de Janeiro, Brazil. By entering these countries in this manner the Chase organization acquired branch networks and hence a broader deposit base, than it could have otherwise achieved. It also obtained institutions which maintained at least a semblance of local identity, which would have been difficult if not impossible to achieve by direct branching.

In June 1967 the Corporations of six individual United States banks, directly or indirectly, held the controlling interest in 16 foreign banks, and in six of these they held virtually all of the outstanding stock. Chemical International Banking Corporation, Continental International Finance Corporation, and Morgan Guaranty International Banking Corporation each holds such control in a bank in Liberia, Belgium, and Italy, respectively. However, it is the three American banks with the largest branch networks--First National City Bank; The Chase Manhattan Bank (NA) and Bank of America NT&SA-- that are the most active in utilizing their Corporations in this manner.

³¹This illustration remains true, even though Chase subsequently purchased a substantial minority interest in The Standard Bank, Ltd., London, and sold its South African subsidiary to The Standard Bank of South Africa, Ltd., a subsidiary of the London Bank. The holding of Chase in Standard is discussed subsequently under Substantial Minority Holdings.



Chase Manhattan Overseas Banking Corporation controls six banks abroad. Originally, these were all located in Latin America, where it now holds the controlling stock of banks in Brazil, Honduras, Peru, and Venezuela.³² Recently it also acquired control of two banks in Europe, one in Belgium and one in Austria.

First National City Bank's subsidiary, International Banking Corporation, has four subsidiary foreign banks, located in Canada, Honduras, Liberia, and South Africa. All except the bank in Honduras are wholly-owned.

Bank of America and its "twin," Bamerical International Financial Corporation, have wholly-owned banking institutions in Germany and Italy and a controlled bank in Spain. It is of interest that in Germany the parent bank also maintains a branch.

Since the parent banks do not operate branches in the countries where they have subsidiaries, except for Bank of America NT&SA in Germany, it is quite obvious that most of these controlled banks function in lieu of direct branches of the parent bank. This is confirmed when one studies the administrative and operational control exercised by the parent bank's International Banking Department. The tendency is for the administrative control of these subsidiaries to be completely coordinated with the operation of the foreign branches. This does not mean that they are treated in precisely the same manner as branches, for their independent and quasi-local character must be recognized, but it does mean that in regard to general policy, administrative control, and reports, they are accepted for what they generally are, namely operations in lieu of direct branches.

³² In the latter part of 1967 the Chase group also acquired control of a bank in Colombia.



Among these three U. S. banks with major foreign branch networks, only The Chase Manhattan Bank (NA) has shown an extreme willingness to take the affiliate route, particularly with majority holdings as contrasted with the wholly-owned subsidiary. There is at least a possibility that there even exists a preference, at least in some circumstances, for the affiliate route over direct branching. During the past three years, while Chase entered four countries via the affiliate route, Bank of America NT&SA entered the same four countries with direct branches.

Substantial Minority Holdings³³

The present substantial minority holdings first appeared in 1960 and for four years were found to only a small extent in Africa and in the Near East. Only since 1963 have they shown a sizable dollar value, but have grown rapidly, particularly with two large investments made in 1965. Recently, 16 Corporations held 27 direct investments of this type covering most of the world except the Far East and the South Pacific.

What constitutes a truly "substantial" or influential minority holding naturally depends on both size and how widespread the balance of the shares are held. As has been noted, they are here arbitrarily said to be greater than 10 per cent and no more than 45 per cent. In practice there is little doubt that some of the smaller holdings in this range are far more influential in the management of the foreign bank, than are larger holdings in other banks. Different functions of an investment can require different degrees of influence and thus there is a considerable variety of ways in which these holdings have been utilized.

³³Over 10 per cent but no more than 45 per cent.



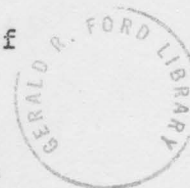
The Corporations of the three banks with major foreign branch-subsidary systems have a total of eight investments representing substantial minority interests. These Corporations, Bank of America, Chase Manhattan Overseas Banking Corporation, and International Banking Corporation, have among others such holdings in Societe Financiere pour les Pays d'Outre-Mer, Geneva, The Standard Bank Ltd., London, and Banque Internationale pour l'Afrique Occidentale, Paris, respectively, each of which has a network of branches and/or subsidiary banks throughout various countries in Africa. There is no general overlapping with the American banks' branches or subsidiaries; the Chase group actually having sold their branch in Nigeria and subsidiary in South Africa to the Standard organization. In all instances, these investments are in lieu of branches, although they certainly cannot be said to be a part of the bank's foreign branch-subsidary system. The same is probably also true of Bank of America's interest in World Banking Corporation, Nassau, Bahamas.

Two other banks with branches other than just in London, Continental Illinois National Bank and Trust Company of Chicago and Morgan Guaranty Trust Company of New York, each holds four such interests through their Corporations. These banks also have smaller minority holdings of substantial value and in no case is there any overlapping with branches. Additionally, Bankers Trust Company, with branches only in London, indirectly holds substantial minority interests in banks in Liberia, Belgium, and Germany and four smaller minority holdings of banks in Africa. All of these investments, while definitely not a part of a branch network, do appear to some extent to be in lieu of branches, giving the parent bank and hence its customers many of the services and benefits which a branch might give.



Of the remaining 10 banks whose Corporations have substantial minority interests in foreign banks only 3 have, or have been authorized to have, foreign branches, all in London. However, with one possible exception, their investments do not appear to be in lieu of foreign branches, although they may fulfill some of the functions that a foreign branch might perform for the parent bank.

The exception is Mellon Bank International's investment in Bank of London and South America, Ltd. ("BOLSA"), London. It illustrates how a bank without foreign branches may view the benefits of this type of investment. BOLSA has several branches on the European continent and numerous branches throughout South America. It also has a substantial interest in the Bank of London and Montreal, Ltd., Nassau, Bahamas, which has branches throughout the Caribbean area. The situation of this Corporation's parent bank - Mellon National Bank and Trust Company - was similar to that in which many of the large and medium sized American banks found themselves. Most of these banks had never developed truly international banking departments nor direct overseas operations, but maintained what amounted to only a foreign service section. In the late Fifties and early Sixties, these banks recognized that they would have to be able to service adequately the rapidly growing international needs of their customers or very likely face the danger of losing a share of the customers' domestic banking business. However, to establish an adequate overseas operation these banks were faced with both the high initial costs and the almost insuperable task of obtaining experienced staffs in this country and abroad. An alternative to these direct overseas operations is the establishment of a close affiliation with an overseas bank, or banks, which are already functioning. Such a close



affiliation normally requires a participation in the management decisions in the overseas banks and this in turn requires a mutuality of aims and usually a substantial stock interest. Through the establishment of such a close reciprocal working relationship, the American bank cannot only service the foreign needs of its own customers, but can also assist the overseas bank in developing its business. Thus, while such investments do not yield the exact equivalent of foreign branches, they do permit the American bank to offer its customers a scope and quality of service not readily available through regular correspondents. This would appear to be the case in the Mellon-BOLSA relationship.

One special situation should be mentioned in passing, namely the holdings of 35 per cent of the stock of the Banque Europeene de Financement, Paris, France, by each Fidelity International Corporation and Wachovia International Investment Corporation. Here two American banks share control of a foreign bank. Neither of the parent banks has overseas branches and both have established truly International Banking Departments in the present decade. Since these investments were made fairly recently, there has not yet been time to evaluate the functions that these holdings will fulfill, but at this point it appears to be more of a door to the Euro-dollar market than a true branch operation.

The remaining holdings of substantial minority interests in foreign banks seem more closely related to some of the functions of smaller minority interests, that are discussed in the next subsection.

Smaller Minority Interests

This type of investment in commercial banks is of relatively recent origin, none having been made until 1960, and there are still none in the "eastern world," and few in Latin America.

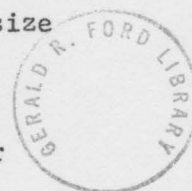


The largest number are in Africa, largely the result of the formation of local banks through the spin-offs of branches of French and Belgian banks, but the largest dollar volume by far has been in Europe.

Bankers International Corporation and Morgan Guaranty International Banking Corporation each holds a number of this type of investment. As mentioned in the preceding section, these particular investments appear to be in lieu of branches.

The balance of these minority investments appear to be more in the order of strengthening correspondent relations. As previously mentioned, some of the substantial minority interests are also fulfilling this same function. One factor influencing the making of such larger investments is no doubt the enactment of the Interest Equalization Tax, which has required since the summer of 1963 the payment of at least 15 per cent tax on many foreign stock investments of less than 10 per cent.

The precise manner in which correspondent relations were expected to be assisted through these minority investments is not always completely clear, nor is it yet possible to judge their overall success, or lack thereof. In general, the holdings usually have been sufficient in size to carry a directorship with them and it is easy to visualize the possible advantageous position that a correspondent might gain under this arrangement. The director would be in a position to assist the stockholding bank and its customers in relations with the local management, perhaps even to the extent of getting special treatment. On the other hand, the director would also be in a better position to understand the local bank's problems, and the manners in which the stockholding bank might be able to be of assistance. However, in at least some instances it appears that the anticipated benefits of an equity holding



have been disappointing. A judgment of the value of collateral benefits is difficult at best and where these difficulties are compounded by the problems of newly independent nations additional time is necessary to judge the utility of many of these investments.

Specialized Functions

There are two types of investments in banks or bank-related companies that have highly specialized functions; the Bahamian trust companies, and other institutions utilized as an entree to the Euro-dollar market. The latter has usually taken the form of specialized finance companies, and while some investments in banks undoubtedly also come within this specialty, e.g. the holdings in Banque Europeene de Financement by The Fidelity International Corporation and Wachovia International Investment Corporation, the analysis of this type of specialized function falls more logically in the following section.

In recent years banking and trust operations in the Bahamas have become of increasing interest to American banks. With the advent of the Interest Equalization Tax and the voluntary foreign credit restraint program, a large volume of funds that formerly went to accounts in the United States have been diverted elsewhere. Thus, these funds avoid the restrictions which have been or might be placed on them if kept in the United States. Funds generated in Latin America in general, and the Caribbean area in particular, have tended to be placed in the Bahamas, and to some extent in Panama. For various reasons a number of the owners of these funds prefer placing them elsewhere than in a branch of an American bank. Thus, due to the Bahamas' liberal banking laws, as well as the lack of foreign exchange restrictions, a number of institutions have been established to specialize in the handling of this business.



As early as 1961 the two largest New York City banks had established wholly-owned trust companies in the Bahamas, and another New York bank held a minority interest in a similar organization. As the situation referred to above developed, the institutions in the Bahamas were quick to take advantage of the new and growing business. Additionally, other American banks became increasingly interested in establishing an operation in the Bahamas. This affords them the means of retaining funds that are no longer being placed in the States and maintaining contact with these customers. With these funds, and others that can be tapped in the Euro-dollar market, the banks are able to service indirectly a portion of the borrowing needs of their customers abroad. With these increasing opportunities it is apparent that at least some of the Corporations, through their Bahamian subsidiaries and affiliates, are going still further afield in seeking new business, including such places as Australia, New Zealand, and the Far East. It seems likely that this growth will continue at least until such time as the United States is in a position to relax the present balance of payments restrictions.

Investments in
Finance and Investment Companies

Included in this classification are all organizations involved in the financial and investment business, except for commercial banks and their related companies. Investments in such financial companies fulfill as broad a range of purposes for the parent banks as the range of operations encompassed by these enterprises and the variety of countries in which they operate. The investments necessary to achieve such purposes are likewise diverse and range from wholly-owned subsidiaries to very small minority interests.



In the early 1950's only a single investment was made in an overseas financial company, namely a newly formed Latin American investment house.³⁴ By the beginning of 1960 such investments still consisted of only 4 minority interests and 2 wholly-owned subsidiaries. However, during the 1960's there has been a very rapid increase in this type of investment by the Corporations, so that by mid-1967 there were 188 such investments totaling over \$70 million. Of this amount, over 40 per cent was in small minority holdings and over 25 per cent in wholly-owned subsidiaries, with the balance almost equally divided between majority controlled and substantial minority interests. Almost half of the small minority interests were in Latin America, and the wholly-owned subsidiaries were largely in the Bahamas, Bermuda, and Canada.

Types of Financial Companies

Although the range of operations of the finance companies invested in is almost limitless, they fall within three general categories: wholesale or development financing and investment, specialty financing, and counseling on financial and investment matters. Excluded from this commentary are the wholly-owned subsidiaries which act as the parent's "alter-ego" as they are discussed in a later section.

The wholesale type of operation is here considered to consist of those companies which offer a number of types of financing, which may include short- medium- and long-term loans, equity participations, and underwriting facilities for debt and equity obligations. They usually do not offer instalment or other such specialized financing.

³⁴ There was also an additional investment in a United States based financial institution.



The most common type of investment in this category has been the development finance company. The distinguishing feature of these companies is that, while not eleemosynary organizations, the application of their resources is dictated more by the developmental needs of the national or regional economy rather than purely by the demands of the market. Many of these are sponsored by the governments of developing countries, and such investments were among the first made by the Corporations in financial enterprises. Many of these government-sponsored companies have received assistance from the International Finance Corporation both in the form of loans and equity participation. While most were formed with the purpose of aiding in the development of a domestic industrial base, others have also assisted the improvement of agriculture, fishing, mining, etc. Two of the best known companies in this subcategory are Industrial Credit and Investment Corporation of India, Ltd. ("ICICI") and Pakistan Industrial Credit and Investment Corporation, Ltd. ("PICIC").

The private development finance companies are of two basic types, namely the national and international. The nationally-oriented private development finance companies are often given specific encouragement through special tax concessions, either on the company's own tax liability or on the tax liabilities arising from the company's obligations, or both. While such companies are found elsewhere, they naturally tend to be more numerous where they have these advantages, such as in Spain. Included in this subcategory are the "financieras" found in many Latin American countries--particularly Colombia, the Spanish "industrial banks," and the "development banks" found elsewhere. One of the better known of these national companies is the Private Development Corporation of the Philippines, whose stock is held by several of the Corporations.



By far the best known of the international private development finance companies is ADELA Investment Company, S. A. While this is a Luxembourg corporation, its operating office and all of its investments and loans are in Latin America. It has one of the most prestigious list of stockholders and directors of any company in the world. Fifteen of the Corporations hold stock in ADELA, and the Chairman of one is Vice Chairman of ADELA.

As of mid-1966, the end of its first complete fiscal year, ADELA had capital accounts of \$35 million and available loans and lines of credit of \$26 million. It had made loan-equity commitments to 44 companies, 29 of which were new, in 14 different Latin American countries, for a total of virtually \$26 million. These companies' fields of operations ranged from development finance companies and agriculture to the manufacture of capital goods and chemical products. Since these commitments had an initially slow rate of disbursements, ADELA made heavy temporary investments in short- and medium-term notes of issuers from 9 Latin American countries.

ADELA is not the only development finance company, government-sponsored and private, that has more than one of the Corporations among its stockholders. Often such investments are considered advisable if the parent bank is to participate in the international banking of that country, this being especially true where the participation is to be in the form of a branch, and the company is government-sponsored.

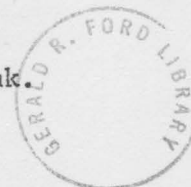
Besides the development finance companies there are also wholesale financial companies which operate in the general market and do not restrict their operations in relation to the developmental needs of the economy. While some of these companies may restrict their operations



to a given country, they more commonly have operations that are international in character, although often concentrating on a given geographic area. In contrast to the development finance companies, which are found primarily in the developing countries, these general finance companies are more often located in the developed countries, although some extend financial assistance to developing areas.

Investments in such companies in Western Europe have shown considerable growth since the development of the Euro-dollar market, and particularly subsequent to the inauguration of the voluntary foreign credit restraint program in 1965. These companies usually extend longer-term financing than banks, and can also take equity participations and engage in underwriting. It is not unusual for more than one Corporation to invest in this type of finance company, although the multiplicity of Corporations with such investments is not as frequent as was noted in the development finance companies. Some companies in this group are wholly-owned subsidiaries, and are also discussed in the section on "alter-ego" subsidiaries.

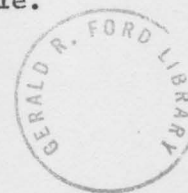
Pure investment companies seem to fit more nearly into this wholesale category than one of the others. These organizations give financial assistance solely through the purchase of shares of stock. Investments in this type of financial enterprise have primarily arisen where the collateral contacts were considered to be of benefit to the parent bank. Thus, in the case of Uganda Crane Industries Ltd., which has some foreign stockholders, the company is controlled by Uganda Development Corporation, a wholly-State-owned development finance company. Uganda Crane's purchase of shares in industrial and agricultural affiliates from Uganda Development Corporation, gave the latter organization additional



funds with which to carry on its various projects. A similar situation occurred when stock investment companies were formed by Spanish banks in order to divest themselves of certain industrial stockholdings in accordance with the revision of the Spanish banking law. Thus, in both such instances not only was an investment considered economically sound, but it also carried possible collateral benefits in the contacts with the company and other stockholders. Additionally, there is always the possibility that such a company might have available funds to invest in the stock of a customer of the Corporation or its parent bank. Thus far there have not been extensive investments in this type of company.

The specialty type of operations has generally been restricted to one country. Also the companies have usually restricted their operations to a single specialty, e.g. equipment leasing, factoring, or instalment financing--frequently of only one type of product. Where a special product or industry is being serviced there is a tendency for the other stockholders to be associated with that product or industry, and less of a tendency for other Corporations to be stockholders.

An example of a wholly-owned enterprise in this category is The First National Bank of Boston's Corporation Financiera de Boston, S.A.F.y.C. in Argentina. Although the bank has a number of branches in the country, this subsidiary services the automotive industry through the purchase of its instalment paper. Investments in minority interests in companies specializing in the purchase or making of instalment loans have a fairly wide geographic spread, although tending to concentrate more in the developed countries or in those where the currency is reasonably stable. The investments in equipment leasing companies have been primarily in France and the former British Dominions. There are relatively few

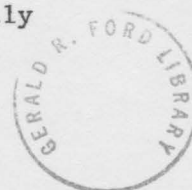


holdings in factoring companies, but included is one world-wide chain which is based on the participation of local banks.

Counseling on financial and investment matters is, of course, a part of the business of all financial companies and banking offices. However, there have been a few investments in companies which have limited their operations to the giving of such advice. These companies specialize in servicing requests for specific information, including the seeking of possible local partners in a given country or area. In one instance the company acts as the investment advisor and distribution manager for a European mutual fund. Thus far, these investments have been primarily of an exclusive character, with no other Corporations as partners, and several are wholly-owned subsidiaries.

Purposes of Financial Investments

The purposes of the parent banks in having their Corporations make this type of investment have been varied. In virtually all cases such investments are viewed as a source of funds. In recent years this has become particularly true in relation to the Euro-dollar market. The parent banks without extensive foreign branch networks often look upon such investments as a method of improving contacts in a country or geographic area, including those with the local government and correspondent banks. Even for those banks with foreign branches, such investments may have a similar purpose in that they are sometimes looked upon as filling gaps in the bank's geographic coverage. Furthermore, in the case of government-sponsored development finance companies, investments are frequently considered politically advantageous when the parent bank is engaging in other financial operations in the country, especially where these operations include direct branches.



Source of Local Currency. The finance companies make an attractive investment for the banks' Corporations because of their ability to generate local funds. This is often true regardless of whether the bank has a branch situated in that country or not. For banks without a branch, the company can offer an alternative to arranging loans through a correspondent bank. It may also be a means of obtaining loans not otherwise available, such as term loans and the discounting of instalment paper. Even for banks with local branches, such investments may allow the bank to offer to its customers a greater range in the types of financing, as well as permitting it to tap additional sources of local funds. This is illustrated by The First National Bank of Boston's Argentine subsidiary, which was mentioned earlier.

The finance companies raise their local funds in a number of different ways. While in some of the more developed countries they may sell short-term commercial paper, the more common methods are loans from local banks and the time deposits that many of them are permitted to receive. These deposits are often from commercial companies whose instalment paper they are handling and in at least one instance additional capital leverage was gained by selling preferred stock to those companies whose instalment paper the finance company purchased.

Besides being able to obtain local funds, these companies are often large enough--and with sufficient credit standing--so as to be able to obtain foreign currency loans to assist small local industries in financing their import requirements. This is of particular importance in the developing countries.



Euro-dollar Market. With the development of this, and especially following the establishment of the Interest Equalization Tax and the voluntary foreign credit restraint effort, various banks, through their Corporations, became interested in establishing or participating in companies that could tap this source of funds. These companies have been established in Europe or in key locations, such as the Bahamas. The funds could be sought either through the issuance of debt obligations or the purchase of time deposits. Banks with branches naturally place more emphasis on debt obligations as their branches can obtain the "deposits," but even here there is an interest in obtaining a means of making loans for a longer term than is the custom for commercial banks in the area. Also under the original version of the Interest Equalization Tax, U. S. dollar loans made by the foreign branches with maturities of over a year were subject to the tax. Hence, to be competitive in this area it was necessary at that time to participate in this market indirectly, if the branches were to serve the long term needs of the banks' customers.

There have been instances where long-term Euro-dollar funds obtained by a subsidiary have assisted a bank's Corporation in carrying on with its equity investment program, without affecting the bank's position under the voluntary foreign credit restraint effort.

Besides investments in finance companies some American banks without foreign branches have also made investments in banks, trust companies, or similar institutions in Europe or the Bahamas. They are thus able to participate more directly in the market for Euro-dollar "deposits." These activities can either supplement or substitute for operations based on less direct access to the shorter-term end of this market, or to the long-term portion through the issuance of bonds or debentures by a subsidiary.



Source of Contacts. For banks without branches in the area, finance company investments can supply contacts which can be utilized in several different ways. If the investment is sufficient to permit the election of a director, he may develop contacts among the other directors, the company's operating officers, other stockholders, interested government officials, and the company's principal local banker--which may also be a correspondent. Through them he may discover how the Corporation or its parent can assist either the finance company, some of its customers, or other parties which cannot be adequately serviced locally. He can also see that the bank's customers receive proper consideration by the company in the servicing of their needs, and that the bank receives adequate and proper credit and other information or services when such is requested. Without such a direct contact these same functions can still basically be accomplished, but the flow of such collateral benefits is likely to be somewhat slower.

Alter-ego Subsidiaries

These subsidiaries usually have the same spectrum of services and operations as their parent Corporations, none of which, thus far, has been "engaged in banking." This is true even though some are oriented towards a particular geographic area, such as Latin America or Europe and the holding of equities may be concentrated in the parent. The distinguishing feature of these subsidiaries is that neither their operations nor those of their parent Corporations can really be considered in isolation, as neither will give a true and complete picture. These subsidiaries are not just a portion of the Corporations' activities, but form an integral part of virtually all their activities. Thus, they and their parent Corporations should be viewed only on a consolidated basis. Illustrative of this alter-ego character is the fact



that besides extending credit through loans, one or more of these subsidiaries hold stocks in various banking institutions, finance companies, and nonfinancial enterprises.

The first of this type of subsidiary was Arcturus Investment and Development, Ltd., Montreal, Canada, which was established in 1955 by Chase International Investment Corporation. In 1959 and 1960 similar subsidiaries were chartered in Panama and the Bahamas by Chemical International Finance, Ltd., Philadelphia International Investment Corporation, and Boston Overseas Finance Corporation, although the subsidiary of the last is now inactive. More recently Bankers International Corporation organized a Luxembourg company and in 1967 First Pennsylvania Overseas Finance Corporation established such a company in the Bahamas. Some of these companies were undoubtedly organized with certain tax benefits in mind and the faster build-up of reserves which would result. It is also interesting to note that in the case of Arcturus its name in no way involves that of the parent bank. Recently these companies have been utilized in avoiding or lessening the impact of the Interest Equalization Tax and the voluntary foreign credit restraint program.

Investments in Nonfinancial Companies

Both in terms of number and of cost, direct holdings of equity interests in nonfinancial businesses by the Corporations have remained small. Acquisitions of such holdings are indeed a fairly recent development. Prior to 1961 all of the equity investments of the Corporations were in banks or other companies providing financing or financial



services.³⁵ In that year, however, two small holdings in nonfinancial companies were acquired at a cost of about \$100,000. At the time, all equity holdings of the Corporations had a total cost of \$28.5 million.

As of mid-1967, the Corporations' portfolio of direct share investments in nonfinancial businesses consisted of 45 separate holdings, valued at cost at slightly more than \$5 million. These holdings amounted to less than 2.4 per cent of the value of the aggregate stock holdings of the Corporations.³⁶

Approximately two-thirds of these stock holdings had been acquired in connection with extensions of credit by the Corporations. About half of these were participations in financing arrangements with the International Finance Corporation (IFC). The remaining stock holdings have been acquired under a variety of circumstances including dividends from other investments, uses of blocked currency, and special arrangements to accommodate customers.

All but one of the companies in which shares were directly held operate exclusively abroad, though three were chartered in the United States. Only three companies were located in major industrial nations, the majority of the investments having been made in developing countries, notably in Latin America, and in somewhat more advanced areas such as Spain, Australia, and Puerto Rico.

³⁵American Overseas Finance Company, which had no banks as stockholders, had two small nonfinancial holdings. Since the subject is the utilization of the Corporations by banks, these nonfinancial holdings are omitted from this discussion.

³⁶In addition, wholly-owned finance subsidiaries of the Corporations had 12 holdings which had cost slightly over \$2 million. The bulk of these holdings were concentrated in one subsidiary. Inclusion of these equity investments would not alter the conclusion that investments in nonfinancial businesses are and have remained small.



With a single exception, these investments in nonfinancial businesses were minority holdings and half involved ownership of less than 2 per cent of the outstanding shares of the companies involved.

The Corporations have differed widely in their acquisitions of these interests. Only 5 held more than three equity interests in nonfinancial businesses as of mid-1967 and 30 Corporations had no such holdings. In general, there has been an apparent lack of suitable opportunities for equity participations in nonfinancial companies and this has affected all Corporations. Additionally, a number of Corporations appear to have avoided making such investments: some perhaps because of lack of sufficient expertise in this area, others perhaps because of a belief that equity investments outside the financial field were not appropriate for their bank.

Where they have exercised it, the abilities of the Corporations to acquire equity interests in nonfinancial businesses has proven a useful adjunct to the conduct and furtherance of their parent bank's international operations. The provision for some equity financing has made some credit operations feasible that otherwise would not have been undertaken. For example, some borrowers, in obtaining financing for certain projects, have not wanted, or not been legally permitted, to pay interest rates that alone would be attractive; however, the Corporation in extending the credit has received shares or options to acquire shares at attractive prices, which have supplemented the lower interest rate. In other cases, where the Corporation has organized the financing of a project, shares or stock options have been received as a commission for its services.

A number of these holdings have arisen, as already indicated, from participations in IFC financing arrangements. Most of these arrangements



have involved furnishing a combination of loan and equity capital, although others have included the issuance of stock options in connection with credit extensions. These participations have been particularly attractive to some of the smaller and less aggressive Corporations. The parent banks have been able in this way to establish or enlarge business and customer relations, especially in less developed countries, that might not have been possible within their own organization.

In addition to these direct acquisitions, the Corporations have acquired indirect interests in nonfinancial businesses through their holdings of equities in foreign financial institutions. In the cases where these equities have represented minority interests, the indirect nonfinancial interests so acquired have been small in number and the degree of interest accruing to the investing Corporation has been similarly minor. So far as the Corporations and their parent banks are concerned, their principal interest has been in the foreign financial institutions--be it bank, development finance company, investment bank--and the benefits accruing from that relationship.

Where the direct equity is in a subsidiary there is, of course, a different situation. Where the subsidiary is a financing company the Corporations have apparently enforced virtually the same policies as apply to their own operations. Where the subsidiary is a bank, there are two possible situations--a newly organized institution, and a going concern that has been acquired. In the former situation no subsidiary bank--or for that matter any institution approximating a bank such as a trust company--has acquired nonfinancial equity interests. However, a number of banks, control of which has been acquired by the Corporations, hold previously acquired equity interests in nonfinancial companies.



What the future role of these holdings may be is difficult to judge at this time as many of these subsidiary banks have been acquired fairly recently. Nonetheless, there are some indications drawn from the experience of the past few years, that the Corporations and their parent banks are primarily interested in strong affiliated banks, not local industrial financial empires, and that they will tend to mobilize the subsidiaries' assets to that end.

Joint Ventures

Joint or cooperative ventures between a United States bank--through its Corporation--with one or more other U. S. and/or foreign banks have only arisen in recent years. They are found in their purest form when two institutions hold unequal parts the controlling stock of another enterprise. The situation is less clear where two institutions both have stockholdings in several organizations, some unequal and others perhaps equal. It is even more complicated where one participant in the joint venture also holds stock of the other participant.

A clear example is the 50-50 holdings of Bank of America and Banco de Santander in Banco Commercial para America and Banco Intercontinental Espanol (a development finance company). In this instance it would appear that this partnership does not extend to activities outside of Spain. Another good example is the 70 per cent holding in Banque Europeene de Financement, Paris, France, half of which is held by each Wachovia International Investment Corporation and The Fidelity International Corporation.³⁷ A slightly more complex situation is that

³⁷The parent banks of these same Corporations have also established an Edge Corporation in New York, owned jointly by them and their partners in the French venture, the principals of Zilka and Sons, Inc., New York.



involving Continental International Finance Corporation (CIFC) and Netherlands Overseas Bank (NOB). Each owns 50 per cent of Continental and Overseas Investment, N. V., which holds all of the stock of a Belgian bank; each holds one-third of the stock of the Commercial Bank of Zambia Limited; and each has a small interest in a Spanish industrial bank, Union Industrial Bancaria. Additionally, CIFC holds stock of NOB, and in Banco Atlantico, which has the largest single interest in Union Industrial Bancaria.

In all cases it seems fairly obvious that these investments represent more than a casual working relationship. It would appear that, whether limited to operations in one or several countries, these joint investments amount in practice to partnerships wherein the mutual interests are closely coordinated in a common project or projects. Such ventures can be attractive to all banks where branch or subsidiary operations are inhibited, but elsewhere probably only to those banks without extensive foreign branch networks.

Utilization of the General Consent

A discussion of the equity operations of the Corporations would hardly be complete without some inquiry into the manner in which these acquisitions were made. Under the Regulation, the Corporations can acquire stock in two manners, either with the specific consent of the Board, or under the terms of the General Consent.³⁸ Specific consents, or approvals to exceed the statutory limitations, are almost invariably necessary for substantial investments, due to the limited capital and

³⁸In view of the aims of the Government's Balance of Payments Program, the Board temporarily removed the General Consent provision by amending Regulation K, effective February 8, 1968.



surplus of the average Corporation - less than \$7 million. They are also necessary where a given investment does not fit into the requirements set forth in the General Consent.

In the first four years after the 1963 Revision to Regulation K established the General Consent,³⁹ the Corporations made approximately 400 direct stock acquisitions, over 100 of which were for additional investments. Of the 400 purchases almost 45 per cent were made under the General Consent; however, their total cost of approximately \$12.6 million was only a very small fraction of the total amount invested. Acquisitions that were incidental to an extension of credit constituted almost a third of all those made under the General Consent. Virtually 75 per cent of investments made under the General Consent were in the developing countries, both as regards number and cost, and well over half of the balance was in Australia, the Bahamas, Canada, Spain, and Puerto Rico.

³⁹September 1, 1963, to October 1, 1967.



CHAPTER VII

PROBLEMS AND QUESTIONS RELATING TO OPERATIONS AND SUPERVISION

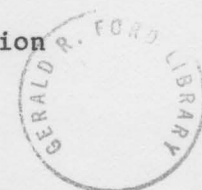
Since the current Regulation was issued over four years ago, the number of Corporations has grown by almost 50 per cent and their total assets and their equity investments have both increased to about three times their previous amounts. Such a rate of growth would prove a severe test for even an experienced area of regulation and supervision. It is not surprising, therefore, that Regulation K has shown some weaknesses and gaps, or that problems have arisen both for the Corporations and for the supervisory authority. These problems are discussed below under three general headings: banking operations in the United States; acquisition of stocks; and miscellaneous. The discussion in several instances is fairly abbreviated. This is because a complete inquiry into some of these problems and the possible solutions, could in itself be a proper subject for a paper.

Problems related to Banking Operations in the U. S.

During the early and mid-1950's the principal problems relating to the Corporations arose from their banking operations. These were solved to a large degree by the 1957 Revision, which detailed what types of deposits and loans would and would not be considered as incidental to the Corporations' international business. The current version made only slight changes.



Since the current Regulation was issued September 1, 1963, the Board has twice published interpretations regarding operations of a banking nature.⁴⁰ The first related to the propriety of Corporations purchasing or selling Federal Funds. In that interpretation the Board stated that such transactions are permissible where they are merely used to adjust the reserve balance, and not as a regular means of investing funds. In the second interpretation the Board held that in calculating deposits in determining aggregate liabilities a Corporation may deduct from gross demand deposits the amounts permitted in Regulation D, "Reserves of Member Banks."



At the present time there do not appear to be any serious problems of a substantive nature regarding banking operations in the United States, either on the part of the Corporations engaged in these activities, or from the supervisory viewpoint. However, there is always the question of whether there is not room for further liberalization of the permissible types of deposits and loans permitted the Corporations. In view of the statutory restrictions on the Corporations' operations in the United States in general, and on the receipt of deposits in particular, the present Regulation appears to represent virtually as liberal an interpretation as is possible. Conceivably there might be room for changes regarding savings deposits; demand deposit accounts used basically for international transactions but occasionally for small domestic payments; and loans made for primarily international transactions, but where a small admixture of domestic items are at times included. However, such

⁴⁰ Interpretations of the Board of Governors of the Federal Reserve System, ¶5700 and ¶5705, p. 481.

changes would at best be minor in character and would raise many of the problems of interpretation and application such as existed prior to the 1957 Revision--both for the Corporations and for the supervisory authorities. Any basic broadening of the Corporations' operations in the United States would seem to depend on statutory changes and these would appear unlikely in face of the strong American tradition against inter-State branch banking.

There are two possible problems which could become acute at some future time. These are the regulatory limitation on aggregate liabilities, and the minimum reserve requirement on deposits in the United States set forth in the statute.

Section 25(a) establishes a limit on a Corporation's liabilities only as to bonds and debentures, but specifically authorizes the Board to limit aggregate liabilities.⁴¹ Since the earliest version, Regulation K has applied to aggregate liabilities the same limit as the statute specifies for bonds and debentures alone, namely, 10 times the Corporation's capital and surplus.⁴² Included in these aggregate liabilities are acceptances outstanding, average deposits, borrowings, guarantees, endorsements, and bonds, debentures and other such obligations. Except for the Board's interpretation permitting certain deductions in calculating deposits, several Corporations would already have had to restrict their operations or ask the Board's permission to exceed this limit. Should a Corporation again approach the limit, the general question could well

⁴¹12 United States Code 615(a).

⁴²12 Code of Federal Regulation Part 211, Section 211.9(c), p. 8.



be raised as to why the Corporations are subject to such a limitation when the banks with which they are competing have no such specific restrictions. Many large banks have aggregate liabilities that run well over 15 times their capital and surplus. Insofar as the Corporations are subject to examination and reports of condition in the same manner as the member banks, such a regulatory limitation on their aggregate liabilities would appear to be no more of a necessity than a similar limitation on all banks.

As to reserves on deposits received in the United States by a Corporation, the statute specifies that they shall be in such amounts as the Board may prescribe, "but in no event less than 10 per centum of its deposits."⁴³ In the Regulation the Board has specified that the Corporations maintain at least the same reserves as required of member banks. At the present time none of the Corporations has sufficient time deposits to cause the 10 per cent minimum to come into effect. At a 4 per cent reserve requirement for time deposits, such deposits would have to constitute over half of total deposits for the statutory minimum to come into effect for Corporations in reserve cities. However, with corporate treasurers' maximizing of earnings and the resulting growth in the importance of time deposits, it is not impossible that this statutory minimum reserve may one day place the Corporations at a competitive disadvantage vis-a-vis the commercial banks.

Problems related to Acquisition of Stocks

As already seen, no other area of the Corporations' activities has had the growth and change as that in their equity holdings. Except for

⁴³12 U.S.C. 615(a).



five holdings in wholly-owned fiduciary and*bank premises companies, all of the Corporations' present stockholdings have been acquired in the past 13 years and two-thirds since September 1963 when the current Regulation was issued.

From the very earliest acquisitions, there have been questions as to the appropriateness of given stockholdings. The basic problem has been to what extent should a Corporation, through stockholdings of even a minority interest, be permitted to do indirectly, that which it cannot do directly. Neither the statute nor the Regulation sheds much light on this subject. Where the investment is basically a means of financing, the question does not appear to be critical. However, the contrary is true where the investment is a means of extending the services offered by the Corporation and its parent bank. The Board's sole published interpretation on stock acquisitions, involved this very question.⁴⁴

The basic question of the Corporations' indirect operations vis-a-vis their permissible direct operations still pervades most problems relating to the Corporations' equity acquisitions. These problems fall into five principal categories, although there are some overlapping areas: operations of subsidiaries; activities in the United States; nonfinancial interest; acquisition under the General Consent; and the value at which equities should be carried on the Corporations' books.

Operations of Subsidiaries

If the statute is cryptic regarding stock investments in general, it is absolutely silent as to the treatment of subsidiaries of the Corporations. If the question of whether a Corporation should be

⁴⁴ Interpretation of the Board, ¶5710, p. 481.



permitted to do indirectly what it is prohibited to do directly, is basic to stock acquisitions in general, it is the heart of the problem of subsidiaries. Where there is a minority interest in a company, that company may be identified with the Corporation, but it can normally never be considered as a part of the Corporation. With a subsidiary, however, it can never be said to be other than a part of the Corporation, and for that matter, the Corporation's parent bank. It has been in this context that all of the Board's specific consents for the acquisition of controlling equities are conditioned on the subsidiary restricting its activities to those permissible for its parent, or permissible if the subsidiary itself had been chartered under the Section 25(a). Virtually the only exception to the broad application of this condition has been as to loans in a local currency.

While the philosophy of this condition seems reasonable, if not inescapable, problems do arise in its practical application. First, when is a company a subsidiary? Second, since local loans are exempted from the limitations of the Regulation, are there other operational limitations--as distinguished from restrictions on basic functions--which can be similarly treated? Last, how can conditions be applied in a completely equitable manner?

When is a Company a Subsidiary? The answer is easy where the Corporation holds a sufficient amount of the company's stock to have control. It is likewise not difficult where the Corporation holds a substantial block of the stock and also has a contract to operate the company. In each of these cases there may be a question of fact, but hardly of policy. Problems are encountered when no one stockholder has absolute control: where two or more Corporations jointly have the



controlling interest, or where a single Corporation clearly has a power of veto - exactly 50 per cent of the voting stock.

In the first of these situations it hardly seems reasonable to allow two or more Corporations to join together in a venture to undertake operations they would not be permitted alone. In the second situation, especially if the other 50 per cent is held by a single foreign institution, the answer is very far from clear. It would seem likely that these cases would have to be treated on an individual basis and that other factors would also have to be considered. Some of these other factors would be the type of operations the company is to undertake, whether they are broad or narrow in scope, the relative position and strength of the stockholders and the limitations of the local laws to which the company would be subject.

Scope of Restrictions on Subsidiaries. The restrictions and limitations set forth in Section 25(a) pertain primarily to operations in the United States. However, the conduct of foreign operations involving the issuance of bonds or debentures, the establishment of branches, or the acquisition of stock, do specifically require Board regulation, consent, or approval.⁴⁵ Thus, the Corporations' activities abroad are subject to some, but not extensive statutory restrictions. The provisions of the 1963 Revision of Regulation K have a generally liberalizing effect on these three areas. While still requiring Board approval for the issuance of long term obligations,⁴⁶ additional branches in a foreign country are permitted giving prior notice to the Board,⁴⁷ and certain

⁴⁵ 12. U.S.C. 615.

⁴⁶ 12 CFR Part 211, Section 211.4, p. 3.

⁴⁷ Section 211.5(b), p. 3.



stock acquisitions are permitted without specific prior Board consent.⁴⁸ The extension of these restrictions to the operations of subsidiaries, would not appear unduly onerous, and would seem necessary if the statutory limitations are not to be circumvented.

However, Regulation K also has other provisions of a limiting character. It severely restricts underwriting when the Corporation is engaged in banking,⁴⁹ and places limitations, based on capital and surplus, on the creation of acceptances, liabilities of one borrower, issuance of guarantees, and a Corporation's aggregate liabilities.⁵⁰ These provisions have varying effects when applied to subsidiaries, depending primarily on the subsidiary's business.

By the very nature of their function, the operations of "alter-ego" subsidiaries would not seem to be prejudiced by any of the restrictions. Similarly those subsidiaries whose activities are confined to nonbanking financial operations would seem to be only slightly affected, except where they might do acceptance financing. The subsidiaries which apparently feel the impact most heavily of this second group of restrictions of Regulation K are the banks. Since the banks are the predominant type of subsidiary and generally the most important by far, this adverse effect is of general concern.

These subsidiary banks usually function in lieu of direct branches of the parent American bank. The direct branches do have legal loan limits, in conjunction with all other branches and their Head Office, but

⁴⁸Section 211.8(a), p. 6.

⁴⁹Section 211.5, p. 3.

⁵⁰Section 211.9(a), (b), and (c), pp. 7-8.



these are based on the parent bank's capital and surplus which is measured in the hundreds of millions of dollars. Both the foreign branches and the subsidiary banks at times need to extend credits disproportionately large in relation to their resources, to customers of the parent bank. An inability to do so can seriously diminish their value to the American bank. It was in recognition of this that the limitations of Regulation K were suspended as to loans in a subsidiary's local currency, and that subsidiaries have been allowed to use their parent Corporation's capital and surplus as a basis for the limitations on creation of acceptances, liabilities to one borrower, issuance of guarantees, and aggregate liabilities. These adjustments appear to have lightened the impact of the regulatory restrictions and limitations, so they do not in general impede the necessary and desirable operations of these subsidiaries. The principal exceptions to this are the restrictions on underwriting, and the limitations on guarantees in those countries where these operations are utilized by the local banking community.

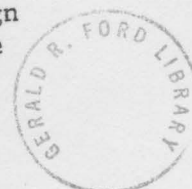
Aside from this general concern with the effectiveness of the subsidiaries' operations, there is an additional consideration which arose recently. In March 1967, the regulatory requirements that Corporations cause their subsidiaries to submit to examination by the Board was removed, due to its extraterritorial implications.⁵¹ This amendment raises the question, at least from the practical viewpoint, as to the desirability of imposing types of limitations which may require examinations to verify conformity.

⁵¹ Law Department, Federal Reserve Bulletin, April 1967, p. 570.



In actual practice the Board has never examined a foreign subsidiary, nor specifically required that it be subject to an audit approved by the Board. The Corporations have naturally required a certain amount of information on the activities of each subsidiary so as to maintain their own supervision of such activities. Thus far, the Board's examiners have found this information to be sufficient for their needs in forming a judgment of the Corporation's overall operations. Therefore, the removal of the regulatory provision for such examinations or audits would not appear to have any direct practical effect. However, problems could arise, should a Corporation fail to maintain on file adequate data regarding a subsidiary's operations. The Board's attitude in this regard was expressed in its press release of March 15, 1967, which accompanied the issuance of the revised version of Regulation M and the above mentioned amendment to Regulation K. In that release the Board stated:

"The Board further expects that member banks (and their foreign branches and affiliates) will conduct their activities, in the United States and abroad, on the basis of high standards of banking and financial prudence. Member banks are expected to make sufficient information available to the Board as will enable the Board to satisfy itself that those standards are being met."



Equal Application of the Condition. To say this is only correct and proper is one thing, to accomplish it is another. Conditions which begin with completely equal application sometimes change to a surprising degree when only minor modifications are made in their terms. Such modifications, of course, reflect intended changes, and usually some inequality of application due to special circumstances. However, the modifications sometimes can cause further inequalities unrelated to the one intended. Such is particularly true where you are dealing with a

group of very similar but yet slightly different organizations such as Agreement Corporations organized under Section 25, and Edge Corporations organized under Section 25(a), and where the latter may or may not be "engaged in banking" with resulting differences in limitations.

Activities in the United States

The statute prohibits the purchase and holding of stock in companies engaging in the general business of buying or selling goods, wares, etc., in the United States or transacting any business in the United States not incidental to its international business.⁵² Additionally, Regulation K prohibits acquisitions where the company is engaged in the business of underwriting, selling, or distributing securities in the United States.⁵³ These indicate that there are certain types of companies operating international businesses in the United States, whose stock may be acquired by the Corporations. A perusal of the possible types of operations of such companies, indicates that the range of possible activities is not large, and is limited primarily to finance and service oriented activities. In practice acquisitions in this area have been very few. However, experience has shown that they raise extremely difficult questions, due primarily to conflicts with traditional American banking practices and the limited operations permitted the Corporations themselves within the United States. It would appear desirable, both from the viewpoint of the Corporations and of the Board, that all acquisitions involving operations in the United States be made only with Board consent.

⁵² 12. U.S.C. 615(c).

⁵³ 12 CFR Part 211, Section 211.8(c)(1)(i), p. 6.



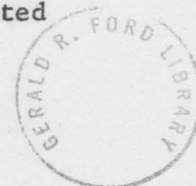
Investments in Nonfinancial Companies

As noted in Chapter V, most investments of this type have been incidental to an extension of credit and virtually all have represented only a minor portion of the company's outstanding stock. As long as these investments are essentially of a financing nature, they would not seem to have any inherent problems, except where operations in the United States are involved. However, it should be noted that in response to an inquiry from the Treasury Department, the Board has stated that the acquisition of more than half of the stock of a foreign company engaged in manufacturing, wholesale selling, or in some similar business would not be appropriate for a Corporation, except in rare instances where the circumstances of some foreign banking or financial operations warranted such an acquisition.

Acquisitions Under the General Consent

Overall experience with acquisitions made under the General Consent has indicated that in part it is too broad in some of its coverage, but also that in other applications it is too narrow.

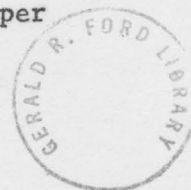
The first of the three subsections of the General Consent--that permitting stock acquisitions which are incidental to an extension of credit--was a recognition that such "sweeteners" are often a part of foreign loan agreements, particularly in the developing countries. The limitation that the extension of credit must be by the Corporation itself is of uncertain derivation, but may well have come from the view that the Corporation is a completely separate organization and should be so treated. Actually, it would seem more logical to view a Corporation as a part of the parent bank's overall international operations, including those of the Head Office and foreign branches, and permit stock



acquisitions incidental to loans by any member of the group. The limitation that the stock acquired may be only that of the borrowing company also appears to be overly restrictive, particularly in those countries where there are numerous interlocking and overlapping company relationships. Frequently a loan may be to a subsidiary, but the more attractive stock for a Corporation is that of the parent holding company, or vice versa.

In practice this subsection of the General Consent has been utilized primarily in acquiring stock in nonfinancial companies and virtually all have represented only a small share of the outstanding stock of the company. However, in at least one instance a wholly-owned subsidiary was acquired by this means, which points up the question of when is a stock acquisition "incidental" to an extension of credit? Under normal circumstances it would seem that the acquisition of a controlling stock interest would not be "incidental" to any credit extension, but would itself be the primary purpose of the transaction. Another questionable case of stock acquisitions being truly "incidental" to an extension of credit, would be the conversion of all convertible bonds held (or all of a loan with an option attached) into stock. In both instances these would seem to be two step acquisitions without any real credit extended.

The second subsection permits the acquisition of less than 25 per cent of the stock of a "foreign bank." This subsection has not been used to any great extent, primarily because acquisitions of bank stock have usually either exceeded the statutory limits, or included 25 per cent or more of the foreign banks' stock, and hence has required a specific consent.



The principal problem in regard to this provision is one of interpretation, namely, what is meant by a "foreign bank." The more logical interpretation would appear to be that "foreign bank" means commercial bank--including English merchant banks and French banque d'affaires--but excluding development banks, Spanish industrial banks, or Latin American "financieras." While these latter institutions may receive certain types of limited deposits, they do not conduct a regular commercial banking business, particularly such as relates to international transactions.

The third and last subsection permits acquisitions of up to \$200,000 which are "likely to further the development of United States foreign commerce." Except for the dollar limitation it is the broadest of the grants under the General Consent and has been the most widely utilized. Unlike the first subsection there is nothing in this provision to prevent imputing the furtherance of U. S. commerce to the purchase of stock in a parent where such furtherance will actually come from a subsidiary's action, or vice versa.

While a few of the investments made under this subsection have been made in nonfinancial companies operating abroad, the majority have been in companies engaged in various phases of financing. In practice this is virtually the only subsection under which this type of acquisition can be made, as relatively few stocks in finance companies have been connected with extensions of credit by the Corporations. Recently, several subsidiaries have been established under this provision. Thus far, the businesses of these subsidiaries have included holding foreign bank premises, investment placement, and the handling of securities.



This provision has not given rise to any problems or questions that are unique to it. This is no doubt due to the breadth of the terminology used--"likely to further."

Besides these problems which are based on the specific provisions of the subsections, there have been two problems of a more general nature, to which some allusion has already been made. The first is that the provisions are too broad in that they permit stock acquisitions (1) representing a controlling interest and (2) in companies with activities in the United States other than those specifically prohibited. Second, the provisions are too narrow in that they include no adequate provision for acquisitions in companies operating a purely financial business.

The problems encountered in stock acquisitions in subsidiaries and in companies with operations in the United States have already been discussed in detail. The combination of the intricate problems in these areas and the possible difficulties encountered in undoing operations--as compared with preventing their occurring in the first place--makes it not only desirable, but virtually necessary, for the Board to have the opportunity to scrutinize such investments prior to their consummation.

In practice the Corporations' investments in nontanking finance companies represent over one-half of all stock investments by number and over one-third by amount. Relatively few of these investments have been connected with any credit extension by the Corporations, by definition the companies are not banks, and recently the average size of such investments has been in excess of \$300,000; hence, they do not normally come within any of the provisions of the General Consent. Excluding subsidiaries, cases of 50-50 ownership, and operations in the United States, experience with investments in financial companies has not



revealed any serious problems, certainly none more involved than in foreign banks. Insofar as the General Consent allows acquisitions of less than 25 per cent of the outstanding stock of foreign banks, it would appear logical to permit similar investments in finance companies, including development finance companies. Such a broadening of the General Consent would permit the Corporations greater flexibility in their operations, and at no apparent risk to basic supervisory control.

There is one additional question of a general nature, namely the need for the parenthetical clause eliminating acquisitions through stock brokers or dealers. In some countries, or in certain situations, stock must be acquired in this manner. If this clause is to prevent the Corporations from "dealing" in stocks, the Board certainly has both adequate means of surveillance via reports and examinations, and sufficient power under its general regulatory and supervisory authority to stop any imprudent operations.

The Proper Carrying Value for Equities

Problems regarding the value at which the Corporations should carry stockholdings on their books can arise in two situations. One is in relation to the condition in the Board's consent for acquisition of stock of subsidiaries. This condition requires that the Corporation not carry the stock on its books at more than the Corporation's proportionate share of the net asset value shown on the books of the subsidiary. The second is in regard to the appraisals of the examiners.

The condition in acquisitions of subsidiary stock has been applied only where there was a premium being paid, or where there was to be an additional contribution by the Corporation to cover prior operating losses of the subsidiary.



The appraisal method for examinations is to find the proportionate net asset value of each stock. If this is less than the Corporation's book value, credit is then given for any proven value of non-ledger assets. If this amount is still less than the book value, an appraisal may be made on the basis of an active stock market quotation, but for no more than the Corporation's book value. Normally no depreciation in a single stock is classified by the examiner as Loss, but only a net depreciation in the entire portfolio. Thus some, if not all, depreciation (other than in a subsidiary's stock) may be offset by appreciation in other stocks. It is generally expected that a Corporation will maintain adequate security valuation reserves to cover such net depreciation.

The need and appropriateness of these writedowns, and their resulting affect on capital accounts, can well be questioned. As an alternative to the use of net asset value, the use of actual cost can muster not formidable arguments, two of which should be noted.

The first is founded on the historical and factual differences between the situations in which the net asset--or book--value requirement originated, and those involved in the Corporations' acquisitions of stocks. The application of the book value basis to Corporations' stockholdings stems from its long use in Bank Holding Company cases. Prior to their being placed under regulatory control in the 1930's, these companies accumulated a considerable amount of "watered" values, many of which grew out of self-dealing situations, usually involving the exchange of stock and not cash purchases. In view of these inflated values, particularly in relation to the prices of the 1930's, the original cost of assets--that is the original book value--was taken as the most logical bench mark. In contrast to this situation the



Corporations' stock acquisitions do not involve any self-dealing, but are the result of arms-length negotiations. Additionally, they do not result from the exchange of stock, but from the payment of cash. Furthermore, the Corporations are subject to examination and close supervision, including specific approval by the Board for all relatively large stock acquisitions.

The second line of argument--based on generally accepted accounting principles--claims that the application of the net book value basis, rather than abolishing distortions, actually creates them not only in the financial statements, but more particularly in the reports on income and earnings. Thus, an immediate charge-off would at the minimum reduce any net capital growth, and could cause an actual loss or impairment of capital, and that this would then be followed by an illusory increase in the rate of capital growth. Such distortions would apply not only to the Corporations, but likewise to their parent banks with which they are consolidated. The crux of this approach is that business activities are no longer considered as separate ventures, but as going concerns and that hence the emphasis has shifted from the balance sheet to the income and expense statement. In view of this, abnormal charges to income, and the possibility of comparing net income to understated assets, should be avoided. The use of cost, rather than net asset value would avoid such abnormal charges.

Miscellaneous Problems and Questions

While none of the following areas appear serious at this time, any of them could arise in a given situation and become critical.



Board Interpretations

As set forth in an earlier chapter there have been four published interpretations by the Board, only one of which pertained to the acquisition of stocks. With the increasing number of investments and since experience has shown that there are certain areas where problems often arise, a freer use of this device would seem to be desirable. Not only would it be likely to prevent types of acquisitions which the Board had already reviewed and felt to be inappropriate, but would place the Corporations on notice of instances where consents might be subject to conditions. Knowledge of such conditions would permit the Corporations to prepare for such contingencies in their early negotiations with the foreign parties.

Underwriting

The statute authorizes the Corporations to purchase and sell bonds and stocks, the latter subject to restrictions, but does not specifically refer to underwriting. However, it has generally been assumed that the statutory language covers these operations. In practice there has been only a minimal amount of experience with underwriting, most of which has been in relation to debt obligations. The rare cases of stock underwriting have all been on a purely standby basis. As is true with all areas where there is a dearth of experience, there exists the possibility of many latent problems. This would seem particularly true of a subject, like underwriting, where there is a strong statutory prohibition against the parent's undertaking such operations.

Guarantees

The 1963 Revision of Regulation K paralleling the revision of Regulation M, authorized the Corporation to issue certain guarantees, but



limited them to 10 per cent of the amount of the Corporation's capital and surplus for any one borrower and in the aggregate to 50 per cent of that amount. Thus far, there have been two questions in relation to these provisions.

One is why a Corporation, not engaged in banking, is permitted to extend unsecured loans of up to 50 per cent of its capital and surplus to a single borrower, but is limited in issuing unsecured guarantees for a single person to only one-fifth that amount--10 per cent of capital and surplus. At the time these provisions were included in the Regulation this was a new authorization of power and therefore the Board had had no experience with its use. In practice this power has not been exercised extensively by the Corporations, although some subsidiaries have a goodly volume of such operations, where they are traditional in the local market, and it is in this regard that this question has usually arisen.

The other question is precisely what is included in these "guarantees"? Prior to this provision--and the parallel one for foreign branches of member banks--banks in general, but particularly their foreign branches, were accustomed to issuing certain Letters of Credit that were virtually the equivalent of a guarantee. Additionally, all banking institutions naturally endorse certain paper with recourse. Whether these types of obligations of the Corporation's should be considered "guarantees" has not yet been indicated.

Summary

The discussion in this Chapter certainly does not exhaust all of the problems related to the Corporations, neither as to those currently encountered, nor as to those that may arise in the future. However, it



does cover the major areas where problems have, or may, be encountered. Viewed individually, or as a whole, these problems, while admittedly troublesome, do not appear to be of a character that impedes the effective utilization of the Corporations by American banks.



CHAPTER VIII

PROSPECTIVE UTILIZATION OF THE CORPORATIONS

The preceding chapters have revealed the extent of the revived interest in Edge and Agreement Corporations. They have shown that since the mid 1950's this has resulted in an increase in parent banks from 6 to 37; the number of Corporations from 6 to 53; those located in a U. S. city other than their parent's, from 2 to 13; and their equity holding from \$2 million to almost \$220 million. They have also shown a statutory history which includes no major changes, and a regulatory background of gradual liberalization which has accelerated in the past dozen years. While a number of problems exist, most are of a technical nature and are not real impediments to the utilization and growth of the Corporations. This is particularly true when one recognizes that such impediments as exist, are due to the Corporations' being a device to breach, to a limited extent, certain strong traditions that are basic to the American banking system, primarily those against inter-State branching, the complete separation of banking and commerce, and the more recent prohibition against combining commercial and investment banking.

The growth in the number, size, and scope of operations of the Corporations is, of course, only a reflection of the increased use of this corporate device by the parent banks. This greater utilization of the Corporations has focused on their two unique powers, namely to be located in a State other than that of the parent bank, and to acquire equity interests. The degree and manner of utilization of the



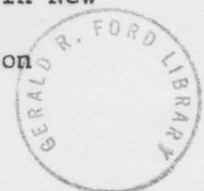
Corporations by the various banks has, of course, varied in accordance with the requirements of the bank's location and its individual type of international operations. However, the experience of the past decade clearly indicates that the utilization of the Corporations has become, in one way or another, a necessary part of virtually all full-fledged international operations of American banks. For those banks outside of New York City, an international banking operation in that center of foreign trade and finance has become increasingly indispensable. For all banks the ability to acquire foreign stocks now appears to be well founded as a necessary part of an international banking and financing operation, whether such acquisitions be of minority interests or control, and whether it be in banks, finance companies, or nonfinancial enterprises. While the 1966 amendment to Section 25 of the Federal Reserve Act and the consequent revision of Regulation M allows member banks to make direct acquisitions of stock in foreign banks, only through the Corporations can the banks acquire equity interests in finance companies or nonfinancial organizations. Furthermore, there has been at least some indication that a number of banks prefer to continue to hold foreign bank stock through their subsidiary Corporations.

In view of the foregoing it seems unlikely that the number, size, and scope of activities of the Corporations are likely to decrease in the future, unless there is a virtual disintegration of international commerce, or the United States should isolate itself from the rest of the world's trade and finance. There remains, however, the question of what are the chances of there being a continuation of their rapid growth such as has occurred.



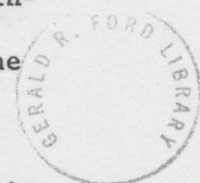
At the end of 1967 there were 103 banks in the United States with deposits of over \$500 million, 45 of which had over \$1 billion. These 103 banks would appear to be a fair approximation of the number of banks, which in the foreseeable future might need, and could support, a full-fledged international banking operation, and hence might require a subsidiary or affiliated Corporation. Special circumstances will no doubt dictate that some smaller banks form a Corporation, either alone or in conjunction with others. However, on the other hand, some of these larger banks may never develop sufficient international business to require a truly international operation and hence the need for a Corporation.

Early in 1968 over one-third of these banks already had a Corporation, or were affiliated with one through a Bank Holding Company. Thus, there appears to be a strong likelihood that additional banks will be forming new Corporations in the next few years, although this likelihood will probably diminish over the longer term, as the number of these larger banks without Corporations diminishes. This conclusion is also borne out by the activities in this area of the 45 largest banks in the United States, which are naturally the prime candidates for utilizing this corporate device. Over two-thirds, 31, already have or are affiliated with Corporations. However, the utilization of the Corporations by these banks is not so widespread when viewed solely from the standpoint of their establishing an out-of-area presence within the United States through the use of the Corporations. Of the 34 largest non-New York City banks only 15 have or are affiliated with a Corporation located in New York, and only one of the 11 New York City banks has a Corporation located outside of the city.



Aside from this likely growth in numbers, it also seems probable that there will be an increase in the size and scope of operations of many, if not all, of the Corporations. About half of all of the present Corporations have been formed in the past six years, and more than half of those located away from their parent started such banking operations within the last three years. Thus, the operations of many of the Corporations already established are still basically in their formative stages and additional growth in size and scope of operations is to be expected. This would seem to be true whether the focus of their operations is on equities or a banking business in the United States.

There are other factors that will also exert an influence, either of a limiting or expansionary character, on the growth of the Corporations. These are the increase, or decrease, in foreign activities of United States commerce and industry in general; the, hopefully, short-term effects of this country's balance of payments problem and the present foreign credit restraint program; and the availability of appropriate equity investments abroad. The possible influence of the first of these is far outside the scope of this paper, but it would seem unlikely that there will be any massive withdrawal by U. S. concerns from their currently extensive foreign operations. The amount that they have invested abroad, would alone seem to be a guarantee of this. As to the foreign credit restraint program, its effect has thus far been to increase the desirability, if not the necessity, for American banks to acquire sources of offshore funds for lending abroad. To achieve this end, equity investments are virtually the only alternative to direct branching. Therefore the restraint program has in this regard supplied an added impetus to the equity investments of the Corporations. However,



the program also has now virtually precluded such investments in Continental Europe. On balance it appears that the program has, and is likely to continue, to accelerate the banks' utilization of the Corporations, particularly their power to acquire stocks.

A vital factor in the growth of the Corporations' equity investments will be the availability of such foreign investments. Those in companies of a nonfinancial nature have usually resulted from extensions of credit and are basically of a temporary character. There would seem to be no particular limit in utilizing Corporations in these operations abroad. The opportunities to invest in various types of foreign finance companies is unlikely to diminish to any great extent, although some of the more lucrative investments may not long be available. Investments in foreign banks might well prove to be a different story, particularly in any given country or area. The number of banks permitted in any country is usually limited. Furthermore, those which a foreigner may control, or even hold stock in, are even more restricted. Thus it would not be surprising if the opportunities for this particular type of equity investment became more limited within a relatively short period.

Judging on all of the information presented, it seems reasonable to believe that the number of Corporations will not decrease, and that on the contrary it is likely to continue to increase fairly rapidly, although in the long run the rate of increase will probably diminish as their number reaches a natural plateau where few if any other banks will be able to utilize them effectively. As to the size of the Corporations, this too will no doubt grow as they gain experience and acquire new customers, or regain old ones. The rate of such growth will, of course, depend primarily on the trend of this country's international trade and



their parent bank's participation in financial transactions abroad. Growth in size will, however, also come to a considerable extent from an increasing scope of operations, particularly in the making of equity investments abroad. The rate of increase in such investments has shown no signs of slackening and as new Corporations are formed and reach maturity there are good reasons to believe that the amount invested in equities will continue to rise at a fairly fast rate.

The above projections could be strongly affected, particularly as to growth in the number of Corporations, should there be a pronounced revival of multi-bank Corporations. This would be especially true should there be so strong a move in this direction that existing Corporations were merged or consolidated. As cited in an earlier chapter of this paper two applications for multi-bank Corporations have recently been received by the Board, one of which has been approved and the Corporation is now open for business. There is, however, no indication that these are the beginning of a wave of such Corporations. Nevertheless, should there be a severe recession in the United States, or a sharp diminution of the country's foreign trade, an increased movement toward joint Corporations could easily develop.

Despite the above caveat, all elements related to the Edge and Agreement Corporations appear likely to increase for several years: the number of banks holding stock in them; the number of Corporations; their size; and their scope of operations and the number and size of their equity holdings.



APPENDIX 1

AMERICAN BANKS AND THEIR INTERNATIONAL CORPORATIONS

as of March 15, 1968

The total capital accounts, as of June 30, 1967--in thousands of dollars--are shown in parentheses for those Corporations opened for business on that date. All are Edge Corporations unless otherwise indicated.

Bank of America National Trust and Savings Association, San Francisco:
Bamerical International Financial Corporation,

San Francisco. (\$3,120)

Bank of America,
New York. (\$59,440)^b

The Bank of California National Association, San Francisco:

Bank of California International Corporation,

New York. (\$2,528)^b

The Bank of New York:

The Bank of New York International Corporation,

New York. (\$2,032)

Bankers Trust Company, New York:

^aBankers Company of New York,

New York. (\$281)

Bankers International Corporation,

New York. (\$8,895)

The Chase Manhattan Bank (National Association), New York:

Chase International Investment Corporation,

New York. (\$17,981)

Chase Manhattan Overseas Banking Corporation,

New York. (\$33,643)

Chemical Bank New York Trust Company, New York:

Chemical International Banking Corporation,

New York. (\$4,088)

Chemical International Finance, Ltd.,

New York. (\$5,461)

The Citizens and Southern National Bank, Savannah:

Citizens and Southern International Corporation,

Atlanta. (\$4,000)



Footnotes are at the end of this Appendix, page 135.

Continental Illinois National Bank and Trust Company of Chicago:

Continental Bank International,
New York. (\$16,794)^b

Continental International Finance Corporation,
Chicago. (\$11,456)

Crocker-Citizens National Bank, San Francisco:

Crocker-Citizens International Bank,
New York.^b

Crocker-Citizens International Corporation,
San Francisco. (\$2,118)

The Fidelity Bank, Philadelphia:

American International Bank,
New York. (\$3,089)^{b c}

The Fidelity International Corporation,
Philadelphia.

The First National Bank of Boston:

Bank of Boston International,
New York. (\$5,251)^b

Boston Overseas Financial Corporation,
Boston. (\$3,458)

The First National Bank of Chicago:

First Chicago International Banking Corporation,
New York. (\$3,191)^b

First Chicago International Finance Corporation,
Chicago. (\$2,180)

The First National Bank of Miami:

^aFirst Foreign Investment Corporation,
Miami. (\$5)

First National City Bank of New York:

First National City Bank (International),
San Francisco.^b

First National City Overseas Investment Corporation,
New York. (\$2,564)

^aInternational Banking Corporation,
New York. (\$33,092)

First Pennsylvania Banking and Trust Company, Philadelphia:

First Pennsylvania Overseas Finance Corporation,
Philadelphia. (\$2,153)

^aVirgin Islands National Bank,
Charlotte Amalie, St. Thomas, V. I. (\$2,616)^b

Franklin National Bank, Mineola, New York:

Franklin International Corporation,
New York.



Irving Trust Company, New York:

Irving International Banking Corporation,
New York.^d

Irving International Financing Corporation,
New York. (\$2,248)

Manufacturers Hanover Trust Company, New York.

^aThe Gallatin Company, Inc.,

New York. (\$295)

Manufacturers Hanover International Banking Corporation,
New York. (\$2,624)

Manufacturers Hanover International Finance Corporation,
New York. (\$2,144)

Manufacturers National Bank of Detroit, Detroit:

Manufacturers-Detroit International Corporation,
Detroit. (\$3,103)

Marine Midland Corporation, Buffalo:^e

Marine Midland International Corporation,
New York. (\$5,178)

Mellon National Bank and Trust Company, Pittsburgh:

Mellon Bank International,
New York. (\$10,229)^b

Morgan Guaranty Trust Company of New York:

Morgan Guaranty International Banking Corporation,
New York. (\$8,350)

Morgan Guaranty International Finance Corporation,
New York. (\$11,409)

The National Bank of Commerce of Seattle, Seattle:

International Bank of Commerce,
Seattle. (\$3,106)^f

National Bank of Detroit, Detroit:

International Bank of Detroit,
Detroit. (\$16,349)

The National Shawmut Bank of Boston:

Shawmut International Corporation,
Boston. (\$2,569)

New England Merchants National Bank, Boston:

New England Merchants Bank International,
Boston. (\$2,565)

The Northern Trust Company, Chicago:

The Northern Trust International Banking Corporation,
New York.^{b d}

Northwest Bancorporation, Minneapolis:^g

Northwest International Bank,
New York. (\$2,490)^b



The Philadelphia National Bank, Philadelphia:
Philadelphia International Bank,
New York. (\$3,759)^b
Philadelphia International Investment Corporation,
Philadelphia. (\$3,989)

Pittsburgh National Bank, Pittsburgh:
Pittsburgh International Finance Corporation,
Pittsburgh. (\$2,146)

Provident National Bank, Philadelphia:
Provident International Corporation,
Philadelphia. (\$2,529)

Security First National Bank, Los Angeles:
Security First International Corporation,
Los Angeles. (\$16,064)

State Street Bank and Trust Company, Boston:
State Street Bank Boston International,
New York. (\$2,595)^b

United California Bank, Los Angeles:
United California Bank International,
New York. (\$5,735)^b

United States Trust Company, New York:
United States Trust Company International Corporation,
New York. (\$2,490)

Wachovia Bank and Trust Company, Winston-Salem:
American International Bank,
New York.^{b c}
Wachovia International Investment Corporation,
Winston-Salem. (\$2,139)

Wells Fargo Bank, San Francisco:
Wells Fargo Bank International Corporation,
New York. (\$12,307)^b

Applications Received
But No Final Permits Issued
as of March 23, 1968

American Fletcher National Bank, Indianapolis:
American Overseas Banking Corporation,
New York.

Republic National Bank, Dallas:
Republic International Company,
Dallas.



Seattle-First National Bank:
Seattle-First International Corporation,
Seattle.

United Virginia Bankshares Incorporated, Richmond:
United Virginia Bank International,
Norfolk.

^a An Agreement Corporation.

^b Operates a banking business.

^c 35 per cent of stock held by the bank.

^d Not yet opened for business.

^e A Bank Holding Company. Lead bank is Marine Midland Grace Trust Company of New York.

^f Operates a banking business, but primarily at branches in Hong Kong.

^g A Bank Holding Company. Lead bank is Northwest National Bank of Minneapolis.

Sources: Overseas Branches and Corporations Engaged in Foreign Banking and Financing, Board of Governors of the Federal Reserve System, Washington, D. C., December 31, 1967, H.2 and K.3 Releases of the Board of Governors.



APPENDIX 2
ESTABLISHMENT OF
SECTION 25 AND SECTION 25(a) CORPORATIONS

The following shows the number and names of Section 25 and Section 25(a) Corporations operating as of December 31, 1954, and those established (opened for business), or closed, for each subsequent year. Also shown is the total number of Corporations in operation at the end of each year.

Section 25 Corporations are indicated by a (*) preceding the name, all others being Section 25(a) Corporations. Where there has been a change in the corporate name, but not in the type of corporation, only the current name is used, except in the case of Bankers International Financing Company, Inc.

	Number in <u>Operation</u>
<u>Prior to 1955</u>	6
*Bankers Company of New York, New York	
*First of Boston International Corporation, New York	
*International Banking Corporation, New York	
*Morgan & Cie., New York	
Bank of America, New York	
Chase International Investment Corporation, New York	
 <u>1955</u>	 7
American Overseas Finance Corporation, New York	7
 <u>1956</u>	 7
 <u>1957</u>	 7
*First of Boston International Corporation, New York (closed)	
American Overseas Finance Corporation, New York (liquidated)	
American Overseas Finance Company	
Bank of Boston International, New York	
 <u>1958</u>	 7
(None)	



	<u>Number in Operation</u>
<u>1959</u>	9
*Chase Manhattan Overseas Corporation, New York	
*Morgan & Cie., New York (closed)	
Bankers International Corporation, New York	
Chemical International Finance, Ltd., New York	
<u>1960</u>	15
American Overseas Finance Company (entered liquidation)	
*The Gallatin Company, Inc., New York	
*Virgin Islands National Bank, Charlotte Amalie, St. Thomas, Virgin Islands	
Bankers International Financing Company, Inc., New York	
Boston Overseas Financial Corporation, Boston	
Morgan Guaranty International Banking Corporation, New York	
Morgan Guaranty International Finance Corporation, New York	
Philadelphia International Investment Corporation, Philadelphia	
<u>1961</u>	16
Chemical International Banking Corporation, New York	
<u>1962</u>	26
*Chase Manhattan Overseas Corporation, New York (closed)	
Bamerical International Financial Corporation, New York	
Chase Manhattan Overseas Banking Corporation, New York	
Continental Bank International, New York	
Continental International Finance Corporation, Chicago	
First Chicago International Banking Corporation, New York	
First Chicago International Finance Corporation, Chicago	
First National City Overseas Investment Corporation, New York	
First Pennsylvania Overseas Finance Corporation, Philadelphia	
Manufacturers Hanover International Banking Corporation, New York	
Manufacturers Hanover International Finance Corporation, New York	
United California Bank International, New York	
(Irving International Banking Corporation, final permit, but not yet opened for business as of March 15, 1968).	
<u>1963</u>	35
*Wells Fargo Bank International Corporation, San Francisco	
The Fidelity International Corporation, Philadelphia	
International Bank of Commerce, Seattle	
International Bank of Detroit, Detroit	
Irving International Financing Corporation, New York	
Manufacturers-Detroit International Corporation, Detroit	
Marine Midland International Corporation, New York	
Mellon Bank International, Pittsburgh	
Northwest International Bank, New York	



	Number in <u>Operation</u>
<u>1964</u>	37
*Wells Fargo Bank International Corporation, San Francisco (closed) Bankers International Corporation, New York (closed) Crocker-Citizens International Corporation, San Francisco Pittsburgh International Finance Corporation, Pittsburgh Provident International Corporation, Philadelphia Wells Fargo Bank International Corporation, San Francisco (Bankers International Financing Company, Inc., New York, changed its name to Bankers International Corporation, New York)	
<u>1965</u>	41
Bank of California International Corporation, San Francisco Citizens and Southern International Corporation, Atlanta State Street Bank Boston International, New York Wachovia International Investment Corporation, Winston-Salem	
<u>1966</u>	45
The Bank of New York International Corporation, New York New England Merchants Bank International, Boston Shawmut International Corporation, Boston United States Trust Company International Corporation, New York (Bank of California International and Mellon Bank International moved their head office to New York.)	
<u>1967</u>	51
Crocker-Citizens International Bank, New York *First Foreign Investment Corporation, Miami First National City Bank (International), San Francisco Franklin International Corporation, New York Philadelphia International Bank, New York Security First International Corporation, Los Angeles (Wells Fargo Bank International Corporation moved its head office to New York) (The Northern Trust International Banking Corporation, New York, final permit, but not yet opened for business as of March 15, 1968.)	
<u>1968</u> (as of March 15, 1968)	52
American International Bank, New York	



APPENDIX 3

ASSETS, LIABILITIES, AND EQUITY HOLDINGS OF
EDGE AND AGREEMENT CORPORATIONS
1954 - 1967

1. Source.

All statistics were derived by the writer from Reports of Conditions filed by the Corporations with the Board of Governors of the Federal Reserve System. Data are as of December 31. of each year, except for 1967 as of June 30. Where necessary, deletions have been made to preserve confidentiality.

2. Adjustments

Number of Corporations. The spreads of assets and liabilities include not only operating Corporations, i.e., those opened for business, but usually those for which a final permit had been issued, but which had not yet opened for business. For the years 1962-1965 inclusive, there was one such Corporation, in 1966 there were four, and in June 1967, there were three.

Equities. These are generally shown at original cost and include investments in subsidiaries in the form of convertible debentures and non-interest bearing loans. Federal Reserve Bank stock and non-conforming stockholdings are excluded and carried under Other Assets. Equities acquired prior to 1955 are shown at net book value, when any write-down had been due to currency devaluation or reflected depreciation in real estate.

Security Reserves. Included are all security valuation reserves, both allocated and unallocated, as shown on the Corporations' reports.

Customers' and Corporations' Liability on Acceptances. Included are liabilities on Deferred Payment Letters of Credit which are no longer contingent insofar as the goods had been delivered.

3. Geographic Divisions used in Equity Spreads

Africa - the entire continent as commonly understood;
Asia and the Near East - the entire area from the eastern shore of the Mediterranean (including European Turkey) to the Pacific Ocean, including Japanese, Philippine, and the East Indian archipelagoes;
Australia and New Zealand;
Bahama Islands, Bermuda, and Canada;



Europe - Continental Europe, the Mediterranean islands appertaining thereto, and the British Isles; includes Finland, but excludes that part of Turkey which is on the continent;

Latin America - the entire western hemisphere lying south of the United States, but excluding U. S. possessions and the Bahama Islands;

United States and Possessions - includes Trust Territories, Puerto Rico and the U. S. Virgin Islands;

"Developed" Countries - include the following, by area:

- Africa - only the Republic of South Africa,
- Asia and the Near East - only Japan and Hong Kong,
- Australia and New Zealand - both,
- Bahamas, Bermuda, and Canada - all three,
- Europe - all, except Finland, Greece, and Portugal,
- Latin America - none, and
- United States and Possessions, all;

"Less Developed" Countries - includes all others; and

No investments have been made within the area of the Sino-Soviet areas.

4. Geographic Classification of Equity Investments

Equity investments have been classified geographically according to the location of their head office, except where their business is predominantly in another geographic area when it has been classified according to its business location. Example: ADELA Investment Company, S.A., Luxembourg, has been included in Latin America.

5. Business Definitions

The definitions of the businesses used are those in common usage with the following possible refinements:

Commercial Banks (Banks) - include merchant banks, banque d'affaires, and in one case a "foreign trade bank," but do not include purely "investment banks," or "industrial banks" or "financieras";

Realty Holding Companies - bank, or branch premises holding companies only;

Development Finance Companies - include "industrial banks," most "financieras," development banks and development companies, government controlled and private;

Finance and Investment Companies - include investment banks and companies, and companies engaged in general finance, equity holding and underwriting, factoring, instalment or retail sale financing, equipment leasing, investment/investor research, or any combination thereof; and

"Other" Companies - includes those in any other types of business, specifically including insurance and warehousing.



APPENDIX 3 (continued)

EDGE AND AGREEMENT CORPORATIONS

ASSETS 1954 - 1967

(Amounts in thousands of dollars)

Year	No. of Corps.	Cash & Due from Banks	U. S. Govts.	Other Bonds	Equities	Security Reserve	Loans	Loan Reserve	Cust. Liab. Acceptances	Fixed Assets	Other Assets	TOTAL ASSETS
1954	6	69,901	61,849	15,075	2,004	(192)	71,462	(807)	11,155	176	1,293	231,916
1955	7	67,982	54,953	21,163	3,956	(547)	93,077	(1,107)	8,967	348	3,862	252,654
1956	7	148,414	58,019	11,712	3,980	(582)	144,703	(1,624)	28,438	579	7,345	400,984
1957	7	126,275	40,654	14,151	16,002	(1,243)	189,957	(2,321)	39,307	970	5,275	429,027
1958	7	165,442	41,903	12,056	16,466	(1,882)	193,342	(3,268)	41,170	828	5,515	471,572
1959	9	142,814	31,879	4,791	20,479	(2,664)	195,705	(4,189)	27,784	3,539	7,718	427,856
1960	15	229,615	40,794	10,405	26,353	(2,983)	218,820	(3,938)	24,941	3,604	2,566	550,177
1961	16	194,104	29,259	6,427	28,487	(4,472)	286,957	(4,476)	45,416	4,725	6,523	592,950
1962	27	236,361	40,872	11,414	48,816	(6,311)	288,608	(4,961)	41,103	4,447	5,007	665,356
1963	36	228,438	28,126	9,492	68,992	(11,589)	255,221	(5,659)	54,923	4,018	3,426	635,388
1964	38	398,794	20,379	8,472	90,891	(14,496)	309,554	(7,410)	73,218	3,986	5,284	888,672
1965	42	403,060	27,346	9,042	146,314	(17,597)	371,060	(7,825)	72,617	3,989	8,136	1,016,142
1966	49	604,593	32,626	20,978	199,588	(20,815)	473,101	(7,939)	69,472	4,499	11,501	1,387,604
6/67	51	808,553	32,750	34,895	218,904	(16,991)	459,309	(7,729)	81,735	4,535	10,215	1,626,176

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APPENDIX 3 (continued)

EDGE AND AGREEMENT CORPORATIONS

LIABILITIES 1954 - 1967

(Amounts in thousands of dollars)

Year	Total Deposits	(Memo: Time Deposits)	Bor- row- ings	Liab. on Accept- ances	Other Liab.	Capital	Surplus	Undi- vided Profits	Contin- gency Reserves	Total Capital Accounts	TOTAL LIABILITIES
1954	170,973	28,561	3,092	12,710	4,122	20,498	14,683	5,662	176	41,019	231,916
1955	179,583	31,012	4,207	10,751	5,689	28,498	17,783	5,967	176	52,424	252,654
1956	290,449	95,784	11,821	32,944	8,082	31,498	19,783	6,288	119	57,688	400,984
1957	275,970	39,701	21,433	42,879	10,630	51,998	18,883	7,116	118	78,115	429,027
1958	309,751	62,047	29,853	43,074	8,925	51,998	19,083	8,770	118	79,969	471,572
1959	292,079	79,831	17,413	28,447	5,091	58,298	20,283	6,216	29	84,826	427,856
1960	425,482	135,431	1,486	25,991	5,984	62,758	20,539	7,000	937	91,234	550,177
1961	433,609	121,365	2,054	46,818	12,248	66,403	20,819	9,224	1,775	98,221	592,950
1962	459,356	108,188	4,448	42,537	8,956	104,248	34,101	9,955	1,755	150,059	665,356
1963	383,502	56,852	10,145	57,081	4,754	130,350	39,001	10,016	539	179,906	635,388
1964	580,779	75,590	27,222	75,009	5,320	146,308	44,994	8,690	350	200,342	888,672
1965	654,139	131,831	25,277	73,640	8,689	171,558	77,085	4,298	1,456	254,397	1,016,142
1966	881,181	120,058	107,638	77,555	9,699	212,218	89,420	8,270	1,623	311,531	1,387,604
6/67	1,078,115	141,091	94,016	84,609	9,550	244,693	91,961	11,661	11,571	359,886	1,626,176

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APPENDIX 3 (continued)

EQUITY HOLDINGS OF EDGE AND AGREEMENT CORPORATIONS

GEOGRAPHIC DISTRIBUTION - Showing: COSTS (thousands of U.S. dollars-equivalent)
NUMBER OF HOLDINGS (in parenthesis)

Year	Africa	Asia and Near East	Australia, N. Zealand	Bahamas, Ber- muda, Canada	Europe	Latin America	U.S. Ter- ritories	Totals
1954	-	-	-	-	622 (6)	* (1)	* (1)	2,004 (8)
1955	* (1)	* (1)	-	* (1)	719 (6)	* (2)	* (1)	3,956 (12)
1956	* (1)	* (1)	-	* (1)	767 (6)	* (1)	* (1)	3,980 (11)
1957	* (1)	* (2)	-	* (1)	12,664 (8)	* (1)	* (1)	16,002 (14)
1958	* (2)	* (2)	-	* (1)	12,561 (8)	166 (3)	* (1)	16,466 (17)
1959	2,332 (3)	628 (3)	-	* (2)	12,561 (10)	166 (4)	* (1)	20,479 (23)
1960	2,781 (7)	1,407 (7)	-	* (2)	12,842 (12)	1,662 (3)	* (1)	26,353 (32)
1961	4,089 (10)	1,576 (8)	* (2)	7,767 (5)	13,053 (15)	1,817 (6)	* (1)	28,487 (47)
1962	7,047 (19)	2,192 (14)	* (3)	11,827 (6)	14,075 (23)	13,366 (20)	* (2)	48,816 (87)
1963	8,482 (26)	4,269 (36)	* (3)	16,031 (8)	24,528 (42)	14,834 (26)	* (2)	68,992 (143)
1964	11,122 (37)	7,245 (53)	1,081 (5)	16,949 (9)	31,033 (50)	23,410 (50)	51 (3)	90,891 (207)
1965	33,968 (40)	7,808 (61)	1,184 (7)	25,493 (11)	43,539 (70)	34,207 (68)	115 (3)	146,314 (260)
1966	35,707 (41)	9,736 (68)	7,138 (11)	33,428 (15)	65,106 (85)	48,358 (84)	115 (3)	199,588 (307)
6/67	37,057 (43)	10,474 (72)	8,673 (11)	33,740 (17)	78,026 (93)	50,674 (87)	260 (4)	218,904 (327)

*Data deleted to preserve confidentiality.



APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

GEOGRAPHIC DISTRIBUTION BETWEEN "DEVELOPED" AND "LESS DEVELOPED" COUNTRIES

Year	Developed Countries			Less Developed Countries		
	Amount	Per cent	Number of Holdings	Amount	Per cent	Number of Holdings
1954	*	*	7	*	*	1
1955	2,733	69.1	8	1,223	30.9	4
1956	3,059	76.9	8	921	23.1	3
1957	14,956	93.5	10	1,046	6.5	4
1958	15,414	93.6	11	1,052	6.4	6
1959	19,185	93.7	15	1,294	6.3	8
1960	22,335	84.8	17	4,018	15.2	15
1961	23,480	82.4	26	5,007	17.6	21
1962	30,044	61.5	36	18,772	38.5	51
1963	44,673	64.8	50	24,319	35.2	93
1964	53,435	58.8	64	37,456	41.2	143
1965	71,626	49.0	80	74,688	51.0	180
1966	106,729	53.5	103	92,859	46.5	204
6/67	121,641	55.6	114	97,263	44.4	213

*Data deleted to preserve confidentiality.



APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

DISTRIBUTION BY BUSINESS OF COMPANY INVESTED IN - Showing: COSTS (thousands of U.S. dollars-equivalent)
NUMBER OF HOLDINGS (in parenthesis)

Year	Banks and Bank Holding Companies	Trust Companies	Nominee Companies	Realty Holding Companies	Development Finance Companies	Finance and Investment Companies	Others	Totals
1954	* (1)	* (2)	-	a (3)	-	* (2)	-	2,004 (8)
1955	* (2)	* (2)	-	97 (3)	* (1)	2,476 (4)	-	3,956 (12)
1956	* (2)	* (2)	-	97 (3)	* (1)	2,452 (3)	-	3,980 (11)
1957	12,167 (3)	* (2)	-	437 (4)	* (2)	2,452 (3)	-	16,002 (14)
1958	12,729 (4)	* (2)	-	333 (4)	* (2)	2,452 (3)	* (2)	16,466 (17)
1959	14,000 (5)	* (2)	a (2)	333 (4)	628 (3)	4,952 (4)	* (3)	20,479 (23)
1960	15,182 (10)	841 (3)	a (3)	333 (4)	674 (6)	9,323 (6)	-	26,353 (32)
1961	16,416 (14)	1,784 (6)	a (3)	333 (4)	829 (7)	9,019 (11)	106 (2)	28,487 (47)
1962	29,226 (23)	1,832 (6)	a (3)	402 (5)	1,754 (13)	14,798 (23)	804 (14)	48,816 (87)
1963	42,000 (31)	2,428 (7)	a (3)	504 (5)	6,343 (44)	16,626 (35)	1,091 (18)	68,992 (143)
1964	45,987 (37)	3,609 (8)	a (3)	504 (6)	17,637 (75)	21,368 (54)	1,786 (24)	90,891 (207)
1965	86,853 (51)	4,566 (7)	1 (6)	504 (6)	22,267 (94)	28,509 (65)	3,614 (31)	146,314 (260)
1966	117,863 (61)	10,463 (7)	1 (7)	506 (7)	23,871 (95)	42,304 (87)	4,580 (43)	199,588 (307)
6/67	132,324 (72)	10,463 (7)	1 (7)	844 (8)	25,394 (97)	44,779 (91)	5,099 (45)	218,904 (327)

*Data deleted to preserve confidentiality.

^aAmounts relatively insignificant in terms of the particular unit.



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APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

IN DEVELOPMENT FINANCE COMPANIES - GEOGRAPHIC DISTRIBUTION

Showing: COSTS (millions of U.S. dollars-equivalent)

NUMBER OF HOLDINGS (in parenthesis)

PER CENT of total investments in Development Finance Companies

Year	Africa		Asia & Near East		Australia & N.Z.	Europe		Latin America		Totals ^b
1954	-		-		-	-		-		-
1955	-		* (1)	100%	-	-		-		* (1) 100%
1956	-		* (1)	100%	-	-		-		* (1) 100%
1957	-		* (2)	100%	-	-		-		* (2) 100%
1958	-		* (2)	100%	-	-		-		* (2) 100%
1959	-		.6 (3)	100%	-	-		-		.6 (3) 100%
1960	-	^c	.7 (6)	100%	-	-		-		.7 (6) 100%
1961	(1)	.8	100%	(6)	-	-		-		.8 (7) 100%
1962	(2)	1.1	58.3%	(7)	a (1) a	* (1)	*	* (2)	*	1.8 (13) 100%
1963	(3)	3.0	47.2%		a (1) a	1.4 (8)	22.0%	1.9 (6)	30.5%	6.3 (44) 100%
1964	1.3 (7)	7.1%	4.2 (32)	24.1%	a (1) a	2.9 (11)	16.3%	9.2 (24)	52.3%	17.6 (75) 100%
1965	1.6 (9)	7.0%	4.5 (36)	20.1%	a (1) a	5.0 (15)	22.3%	11.2 (33)	50.4%	22.3 (94) 100%
1966	1.6 (9)	6.6%	4.6 (35)	19.1%	a (1) a	5.9 (15)	24.5%	11.9 (35)	49.7%	23.9 (95) 100%
6/67	1.6 (9)	6.2%	4.8 (36)	19.0%	a (1) a	6.9 (15)	27.2%	12.1 (36)	47.5%	25.4 (97) 100%

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*Data deleted to preserve confidentiality.

^aAmounts relatively insignificant in terms of the particular unit.^bDetails may not add to totals because of rounding.^cCosts and percentages for the two areas are combined in certain years to preserve confidentiality.

APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

IN FINANCE AND INVESTMENT COMPANIES

GEOGRAPHIC DISTRIBUTION - Showing: COSTS (millions of dollars-equivalent)
 NUMBER OF HOLDINGS (in parenthesis)
 PER CENT of total investments in Finance/Investment Companies

Year	Africa	Asia and Near East	Australia, New Zealand	Europe	Bahamas, Ber- muda, Canada	Latin America	U.S. Ter- ritories	Totals ^b
1954	-	-	-	-	-	*(1)*	*(1)*	*(2)100%
1955	-	-	-	-	*(1)*	*(2)*	*(1)*	2.5(4)100%
1956	-	-	-	-	*(1)*	*(1)*	*(1)*	2.5(3)100%
1957	-	-	-	-	*(1)*	*(1)*	*(1)*	2.5(3)100%
1958	-	-	-	-	*(1)*	*(1)*	*(1)*	2.5(3)100%
1959	-	-	-	-	*(2)*	*(1)*	*(1)*	5.0(4)100%
1960	-	-	-	-	*(2)*	1.7(3)17.8%	*(1)*	9.3(6)100%
1961	-	-	*(2)*	*(1)*	*(2)* ^c	1.8(5)20.0%	a(1)a	9.0(11)100%
1962	-	*(4)*	*(2)*	1.2(7) 7.9%	(3) 12.9	87.5% (6)	a(1)a	14.8(23)100%
1963	*(1)* ^c	.8(7)5.1%	*(2)*	1.8(14)10.8%	(3) 13.0	78.5% (7)	a(1)a	16.6(35)100%
1964	(3) 2.5	11.7% (15)	1.1(4) 4.9%	4.2(18)19.5%	(3) 13.6	63.9% (10)	a(1)a	21.4(54)100%
1965	(2) 2.7	9.3% (17)	1.2(6) 4.0%	9.1(21)32.0%	11.3(5)39.7%	4.3(13)15.0%	a(1)a	28.5(65)100%
1966	(2) 4.4	10.4% (22)	6.6(9)15.7%	13.8(29)32.6%	12.5(8)29.5%	5.0(16)11.8%	a(1)a	42.3(87)100%
6/67	(2) 4.5	10.0% (23)	8.2(9)18.2%	14.2(31)31.7%	12.5(8)27.8%	5.5(17)12.3%	a(1)a	44.8(91)100%

See footnotes on page 146.



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APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

IN BANKS AND BANK HOLDING COMPANIES

GEOGRAPHIC DISTRIBUTION - Showing: COSTS (millions of U.S. dollars-equivalent)
 NUMBER OF HOLDINGS (in parenthesis)
 PER CENT of total investment in Banks/Bank Holding Companies

Year	Africa	Asia and Near East	Europe	Bahamas, Ber- muda, Canada	Latin America	U.S. Ter- ritories	Totals ^b
1954	-	-	*(1) 100%	-	-	-	*(1) 100%
1955	*(1)*	-	*(1)*	-	-	-	*(2) 100%
1956	*(1)*	-	*(1)*	-	-	-	*(2) 100%
1957	*(1)*	-	*(2)*	-	-	-	12.2(3) 100%
1958	*(2)*	-	*(2)*	-	-	-	12.7(4) 100%
1959	*(3)*	-	*(2)*	-	-	-	14.0(5) 100%
1960	2.8(7) 17.5%	c *(1)*	*(2)*	-	-	-	15.2(10) 100%
1961	(9) 4.7	28.9% (1)	11.7(4) 71.1%	-	-	-	16.4(14) 100%
1962	(16) 7.4	25.5% (1)	11.6(3) 39.6%	-	10.2(3) 34.9%	-	29.2(23) 100%
1963	(20) 8.4	20.2% (1)	19.7(6) 46.9%	(1) 13.8	32.9% (3)	-	42.0(31) 100%
1964	(24) 10.1	21.8% (2)	22.2(6) 48.3%	(2) 13.8	29.9% (3)	-	46.0(37) 100%
1965	(27) 32.8	37.7% (2)	26.1(12) 30.0%	10.7(3) 12.3%	17.4(7) 20.0%	-	86.9(51) 100%
1966	(27) 34.5	29.2% (2)	42.5(19) 36.1%	11.6(4) 9.8%	29.3(9) 24.9%	-	117.9(61) 100%
6/67	(28) 35.6	27.0% (3)	54.1(25) 40.9%	11.9(5) 9.0%	30.6(10) 23.1%	a(1)a	132.3(72) 100%

See footnotes on page 146.



APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

IN TRUST, NOMINEE AND REALTY HOLDING COMPANIES

GEOGRAPHIC DISTRIBUTION - Showing: COSTS (in millions of U.S. dollars-equivalent)
NUMBER OF HOLDINGS (in parenthesis)

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Year	Trust Companies		Nominee Companies		Realty Holding Companies	
	Bahamas, Bermuda, Canada	Europe	Asia and Near East	Europe	Europe	Others
1954	-	* (2)	-	-	a (3)	-
1955	-	* (2)	-	-	.1 (3)	-
1956	-	* (2)	-	-	.1 (3)	-
1957	-	* (2)	-	-	.4 (4)	-
1958	-	* (2)	-	-	.3 (4)	-
1959	-	* (2)	-	a (2)	.3 (4)	-
1960	-	.8 (3)	-	a (3)	.3 (4)	-
1961	.9 (3)	.8 (3)	-	a (3)	.3 (4)	-
1962	1.0 (3)	.8 (3)	-	a (3)	.4 (5)	-
1963	1.6 (4)	.8 (3)	-	a (3)	.5 (5)	-
1964	2.6 (4)	1.0 (4)	-	a (3)	.5 (5)	a (1)
1965	3.5 (3)	1.1 (4)	a (2)	a (4)	.5 (5)	a (1)
1966	9.4 (3)	1.1 (4)	a (2)	a (5)	.5 (5)	a (2)
6/67	9.4 (3)	1.1 (4)	a (2)	a (5)	.5 (5)	.3 (3)

*Data deleted to preserve confidentiality.

^aAmounts relatively insignificant in terms of the particular unit.



APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

IN "OTHER" COMPANIES

GEOGRAPHIC DISTRIBUTION - Showing: COSTS (millions of U.S. dollars-equivalent)
 NUMBER OF HOLDINGS (in parenthesis)
 PER CENT of total investment in "Other" Companies

Year	Africa	Asia and Near East	Europe	Latin America	Other	Totals ^b
1954	-	-	-	-	-	-
1955	-	-	-	-	-	-
1956	-	-	-	-	-	-
1957	-	-	-	-	-	-
1958	-	-	-	*(2) 100%	-	*(2) 100%
1959	-	-	-	*(3) 100%	-	*(3) 100%
1960	-	-	-	-	-	-
1961	-	*(1)*	-	*(1)*	-	*(2) 100%
1962	*(1)*	*(2)*	a(1)a	.4(9) 53.7%	*(1)*	.8(14) 100%
1963	*(2)*	*(2)*	.3(3) 24.7%	.5(10) 43.3%	*(1)*	1.1(18) 100%
1964	*(3)*	.2(4) 8.9%	.2(3) 12.3%	1.2(13) 65.4%	*(1)*	1.8(24) 100%
1965	*(2)*	.2(4) 5.4%	1.8(9) 51.1%	1.3(15) 36.2%	*(1)*	3.6(31) 100%
1966	.2(3) 3.6%	.3(7) 6.3%	1.3(8) 28.6%	2.2(23) 48.5%	.6(2) 13.0%	4.6(43) 100%
6/67	.2(3) 3.2%	.5(8) 10.4%	1.3(8) 25.7%	2.5(23) 48.7%	.6(3) 12.0%	5.1(45) 100%

See footnotes on page 146.



APPENDIX 3 (continued)

EQUITY HOLDINGS (continued)

DISTRIBUTION BY PER CENT OF OUTSTANDING STOCK OWNED - Showing: COSTS (thousands of U.S. dollars-equivalent)
 NUMBER OF HOLDINGS (in parenthesis)
 PER CENT of total equity investments

Year	90+ to 100 per cent		45+ to 90 per cent		10+ to 45 per cent		Nominal to 10 per cent		
1954	560	(5) 27.9%	-	-	1,444	(3) 72.1%	-	-	-
1955	2,171	(7) 54.9%	-	-	*	(2) *	*	(3) *	*
1956	2,449	(7) 61.5%	-	-	*	(3) *	*	(1) *	*
1957	14,346	(9) 89.7%	-	-	*	(3) *	*	(2) *	*
1958	14,804	(10) 89.9%	-	-	1,270	(3) 7.7%	392	(4)	2.4%
1959	18,575	(14) 90.7%	-	-	1,270	(3) 6.2%	634	(6)	3.1%
1960	22,939	(17) 87.1%	-	-	2,426	(8) 9.2%	988	(7)	3.7%
1961	24,431	(20) 85.8%	-	-	2,065	(10) 7.2%	1,991	(17)	7.0%
1962	29,949	(21) 61.4%	10,704	(4) 21.9%	3,002	(15) 6.1%	5,161	(47)	10.6%
1963	31,094	(23) 45.1%	14,450	(7) 20.9%	10,605	(19) 15.4%	12,843	(94)	18.6%
1964	33,198	(25) 36.5%	15,749	(8) 17.3%	14,414	(35) 15.9%	27,530	(139)	30.3%
1965	45,088	(30) 30.8%	17,547	(12) 12.0%	38,865	(47) 26.6%	44,814	(171)	30.6%
1966	53,663	(36) 26.9%	33,393	(16) 16.7%	64,850	(63) 32.5%	47,682	(192)	23.9%
6/67	53,927	(37) 24.6%	42,999	(18) 19.7%	72,436	(74) 33.1%	49,542	(198)	22.6%

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*Data deleted to preserve confidentiality.



APPENDIX 4

REGULATION K OF THE BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

including

SECTION 25(a) AND EXCERPTS
OF SECTION 25 OF THE FEDERAL RESERVE ACT.

(See back pocket.)



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