

definition, a foreign bank is an institution that is:

(1) incorporated or organized under the laws of a country other than the United States or a political subdivision of a country other than the United States;<sup>24</sup>

(2) regulated as a bank by that country's or subdivision's government; and

(3) engaged substantially in the business of banking.<sup>25</sup>

This definition would also include a provision explaining that, in order to be an institution engaged substantially in the business of banking, a foreign entity must receive deposits to a substantial extent in the regular course of its business, have the power to accept demand deposits, and extend commercial or other types of credit.<sup>26</sup> Thus, this definition would exclude from the exemption foreign companies that are in the business of extending credit but, because they do not accept deposits in the home country, are subject to a less stringent regulatory regime there.

#### Comment Solicited

We solicit comment on the proposed definition of foreign bank as well as on all other aspects of the proposed rule. Here and throughout the release, when we solicit comment, we are interested in hearing from all interested parties, including members of the investing public, representatives of the foreign and domestic banking community, other foreign private issuers and domestic issuers. We are further interested in learning from all parties what aspects of the rule proposal they deem essential, what aspects they believe are preferred but not essential, and what aspects they believe should be modified.

Regarding the proposed definition of foreign bank, should we exclude from the definition financial institutions that extend credit but do not customarily accept deposits in their home jurisdictions, as proposed? Are there other types or characteristics of foreign financial or lending institutions that should be included or excluded from the definition of foreign bank and, if so, why? Is it appropriate to look to Regulation K under the Federal Reserve Act for the proposed definition of foreign bank? Is there another regulation

or law that would be more appropriate and, if so, why?

#### C. The Home Jurisdiction Deposit Insurance or CCS Condition

Proposed Rule 13k-1(b)(1) would establish two alternative conditions. Under the first condition, a foreign bank would be eligible for the exemption if it were subject to a deposit insurance regime in its home jurisdiction. This condition would be consistent with the Sarbanes-Oxley Act by making it more likely that a qualifying foreign bank is subject in its home jurisdiction to a banking regulatory regime that generally addresses the risks that Section 402 was intended to guard against. Moreover, since domestic banks are currently subject to a deposit insurance requirement, adoption of a similar requirement for foreign banks would assist in ensuring that foreign banks are not viewed as advantaged over domestic banks when determining eligibility for the Section 13(k) exemption.

While there appears to be some difference of opinion among foreign banking regulators and economists as to the role of an insurance scheme in ensuring an effective and sound banking regulatory regime,<sup>27</sup> numerous countries have nevertheless adopted some form of a deposit insurance scheme, including approximately 34 European countries, 10 African countries, 8 Asian countries, 4 Middle Eastern countries, and 16 countries from North or South America.<sup>28</sup> Therefore, our proposed home country deposit insurance requirement for foreign banks, if adopted, would likely be satisfied by most foreign banks.

Moreover, we have phrased the deposit insurance requirement in general terms in recognition that there are differences among deposit insurance schemes in the foreign banks' home countries. In the interest of comity, we believe that deference to the foreign banking supervisor regarding the details of its deposit insurance scheme is appropriate.

Proposed Rule 13k-1(b)(1)'s alternative condition would render a foreign bank eligible for the exemption

if the Federal Reserve Board has determined that the foreign bank is subject to comprehensive supervision or regulation on a consolidated basis ("CCS") by its home jurisdiction supervisor. CCS refers to a Federal banking regulatory requirement that provides that, before a foreign bank can establish a U.S. branch or agency or acquire a U.S. bank or commercial lending company, the Federal Reserve Board must determine that the foreign bank is subject to CCS in its home jurisdiction.<sup>29</sup> In order to make this determination, among other considerations, the Board must find that the supervisor in the bank's home jurisdiction receives information on the bank's worldwide operations sufficient to assess the bank's overall financial condition and compliance with laws and regulations.<sup>30</sup>

We recommend establishing a favorable CCS determination as an alternative condition to a deposit insurance requirement primarily in order to accommodate foreign banks located in jurisdictions that lack a deposit insurance scheme yet have received a favorable CCS determination. This alternative would be consistent with Section 402 by rendering eligible for the bank exemption those foreign banks permitted to do business in the United States because the Board has found their home country banking laws and supervision to be sufficiently comprehensive.

By requiring either a home country deposit insurance scheme or a favorable CCS determination, we would ensure that the insider lending exemption would apply only to qualified foreign banks and not to other foreign entities, such as insurance companies or pension funds, that may also be subject to oversight in their home countries. Moreover, by positing a home

<sup>29</sup> See 12 U.S.C. 3105(d)(2)(A) and 12 CFR 211.24(c).

<sup>30</sup> When making this CCS determination, the Board must assess a number of factors, including the extent to which the home country supervisor:

(1) Ensures that the foreign bank has adequate procedures for monitoring and controlling its activities worldwide;

(2) obtains information on the condition of the foreign bank and its subsidiaries and offices outside the home country through regular reports of examination, audit reports, or otherwise;

(3) obtains information on the dealings and relationships between the foreign bank and its affiliate companies;

(4) receives from the foreign bank consolidated financial reports on a worldwide basis or comparable information that permits analysis of the foreign bank's financial condition on a worldwide, consolidated basis; and

(5) evaluates prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis.

12 CFR 211.24(c)(1)(ii).

<sup>24</sup> Under the Exchange Act, the term "United States" includes the District of Columbia, Puerto Rico, the Virgin Islands, and any other possession of the United States. See the definition of "State" in Exchange Act Section 3(a)(16) [15 U.S.C. 78c(a)(16)]. The proposed rule would assume this statutory definition.

<sup>25</sup> See proposed 17 CFR 240.13k-1(a).

<sup>26</sup> See proposed 17 CFR 240.13k-1(a)(3).

<sup>27</sup> See for example, U.S. GAO, "Deposit Insurance: Overview of Six Foreign Systems" (February 1991); and James R. Barth, "Bank Regulation and Supervision: What Works Best?", 11, n. 5 (January 2002), a Basel Committee Working Paper available at <http://www.bis.org/bcbs/events/b2ealev.pdf>.

<sup>28</sup> See Federal Deposit Insurance Corporation, "International Directory of Deposit Insurers" (2000), which is available at <http://www2.fdic.gov/iddi/intguide00.pdf>; and Working Paper 99/54 for the International Monetary Fund, "Deposit Insurance: A Survey of Actual and Best Practices," 30-34 (April 1999) ("IMF Working Paper").