10-1-1979

International Banking and Finance

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Review of Key Provisions of Both State and Federal International Banking Laws for Florida

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In recent years, Miami's reputation as a national and international tourist center has been acquiring a new dimension. Its bilingual population and relative proximity to Latin American markets have stimulated the growth of Miami's foreign trade with Central and South America and have propelled it into an attractive and convenient site for the Latin American operations of U.S. businesses.[1] As a direct consequence, the volume of international business by Miami banks has expanded. A significant share of this international business is attributable to Edge Act corporations established by out-of-state banks for the conduct of international banking.[2] Growing interbank competition and the increased sophistication of their international clients have contributed to the development of Miami as a full-service, specialized, Latin American banking center.

The economic rise of Miami, and hence Florida, both nationally and internationally, prompted the State Government to introduce appropriate banking legislation and provide a regulatory framework for international banking activity. Thus, unlike 1976 when foreign banking legislation was embryonic, 1977 marks the statutory development of Florida's international banking law.

The 1977 Florida foreign banking legislation set out to attain essentially two objectives: (1) to preserve, and, in some instances, enhance the competitive position of domestic banks vis-à-vis foreign banks; (2) to induce, for the first time, the location of foreign banks in Florida and hence to improve the state's competitiveness with such states as California, Georgia, Illinois, Massachusetts, New York, and

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1. Luytjes, *Miami: Coming of Age in International Trade,* MUNDO LATINO 16 (1975).

2. Baer, *Expansion of Miami Edge Act Corporations,* ECONOMIC REVIEW, Federal Reserve Bank of Atlanta, September–October, 1977, at 112. *See also* Baer & Garlow, *International Banking in the Sixth District,* ECONOMIC REVIEW, Federal Reserve Bank of Atlanta, November–December, 1977, at 127.

Washington, which have passed similar legislation in an effort to enhance their attractiveness to the international banking communities.

The legislation of these other states generally permits a foreign banking corporation to operate within state boundaries through five different legal forms of organization,[3] each of which entails a basically different level of operation and regulatory control. These forms, in order of increasing levels and freedom of operations, include the representative office, the agency, the branch, the subsidiary, and the investment company with banking functions. In many cases, a representative office is merely the initial step by which foreign banks enter the United States, subsequently being converted into other types of banking operations. Such an office does not engage in actual banking operations but solicits business for its parent bank. An agency is permitted to carry on general banking business for itself except that it may not accept deposits. A branch may accept deposits and, therefore, can engage in the full service commercial banking business. Whereas each of the preceding forms is a direct extension of a foreign banking institution, a subsidiary is a legally separate banking entity, chartered and functioning in this country as a full service bank, but owned and controlled by foreign banking interests. Investment companies are subsidiaries of foreign banks, chartered to deal in securities and engage in the general banking business (except that they are not allowed to take deposits) and are recognized as banks by state legislation.[4]

Of the aforementioned legal forms of organization for foreign banks, Florida legislation permits only the first two. The following paragraphs examine the legal issues associated with these forms.

Key Sections of Florida's International Banking Legislation

Florida House Bill 1250, enacted into law on June 8, 1977, invites international banking corporations to establish themselves in Florida—effective January 1, 1978—through a representative office or an international bank agency.[5] Further provisions provide for the licensing of those applicants that meet certain requirements which were intended to distinguish Florida's policies from the Caribbean tax-haven banking centers. These requirements include a minimum

3. PEAT, MARWICK, MITCHELL & CO., ESTABLISHING AN OFFICE OF A FOREIGN BANK IN THE UNITED STATES: A GUIDE FOR FOREIGN BANKS (2nd ed. 1977).
4. *See, e.g.*, N.Y. BANKING LAW § 202(a) (MCKINNEY).
5. FLA. STAT. § 659.67 (1977).

net worth ($25,000,000) for the international banking corporation[6] and reciprocity for Florida banks by the corporation's host country.[7] Qualified international banking corporations may be licensed to operate in Florida and may "have only one place of doing business as specified."[8]

As might be expected, the scope of permissible activities under either of these two forms is subject to significant restrictions. The Florida statute provides that the representative office of a foreign banking corporation may not conduct any banking business in the state, but may function "in a liaison capacity with existing and potential customers of [the] international banking corporation and . . . generate new loans and other activities for such international banking corporation which is operating outside of the state."[9] In other words, the representative office may generate loans, deposits, letters of credit and other business for a foreign bank, operating along the same lines as the "loan production," "trust production," or "business production" offices of large domestic banks.

The statute imposes two basic limitations on the activities of an international banking agency. First, it defines the scope of lending that is permissible for a foreign bank agency: "[A banking agency] is authorized to transact only such limited business in [the] state as is clearly related to and is usual in international or foreign business and financing international commerce."[10] The agency is thus authorized to make loans related only to foreign business and commerce and is prohibited from engaging in domestic financing. This domestic limitation seems to have no precedent in the foreign legislation of those states—California, Georgia, Illinois, Massachusetts, New York and Washington—which are actively promoting the growth of their own international financial centers. Moreover, this limitation is academic since the banking agency could circumvent it by booking loans at its home office or at any other of its banking offices operating outside Florida.[11]

The second limitation on the activities of an international banking agency pertains to its non-lending functions. Specifically, "[N]o such international banking corporation shall exercise fiduciary powers or

6. *Id.* at § 659.67(5)(a)(5).
7. *Id.* at § 659.67(4)(b).
8. *Id.* at § 659.67(6)(a).
9. *Id.* at § 659.67(1)(d).
10. *Id.* at § 659.67(6)(c).
11. Doss, *Florida's Invitation to the International Banking Community*, 51 FLA. B.J. 449, 451 (1977).

receive deposits, but it may maintain for the account of others credit balances necessarily incidental to, or arising out of, the exercise of its lawful powers."[12] This provision follows closely the legislation of Georgia and New York and constitutes the basis for the distinction between an agency and a branch of a foreign bank.

As stated in this provision, a foreign banking agency may not accept deposits (domestic or foreign), but it may hold credit balances. The concept of credit balances, new to Florida law, is afforded a definitional framework by the law of other states, such as New York and California.[13] Customer credit balances, frequently referred to as "limited-purpose" deposits, are permissible only as long as they are associated with international transactions; that is, transactions related to the agency's involvement with foreign business and the financing of international commerce. For example, a credit balance may arise as a result of uncollected or undisbursed funds: loan proceeds to customers; proceeds of incoming remittances; proceeds of collections made for customers' accounts; cash collateral or compensating balances from a customer; or funds received from customers to cover currency transactions.

In addition to credit balances, a foreign banking agency may derive funds through acceptances, borrowing, sale of securities subject to repurchase, interbank accounts, participations and standby letters of credit. Of course, supplementary funding will always be available through intrabank transfers; that is, through fund transfers from the home office or other offices of the international banking corporation located outside Florida.

Review of Selected Sections of the International Banking Act of 1978

The legislative framework outlined above was significantly affected in September 1978 by the enactment, at the federal level, of the International Banking Act (IBA).[14] By establishing a federal regulatory framework, this law offers foreign banks a charter from the Office of the U.S. Comptroller of the Currency as an alternative to the state charter.[15] In other words, the stage is set for a vigorous, competitive dual banking system for foreign banks which is expected

12. *See* note 9 *supra*.

13. Baena & Romanchuch, *Banking Law-Survey of Florida Developments*, 32 U. MIAMI L. REV. 763, 768 (1978).

14. 12 U.S.C. § 3101 *et. seq.* (1978).

15. S. REP. NO. 95-1073, 95th Cong., 2d Sess., *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 2827, 2832.

to promote a more liberal approach to the regulation of foreign banking corporations throughout the country.

Section 5.0 of this act permits any foreign bank interested in having offices in this country to be chartered by the Comptroller of the Currency.[16] The bank can then establish itself in any state that it selects (called "home state"), provided that particular state's law does not specifically prohibit such entry.[17] No foreign bank may establish both a federal branch and a federal agency in any state.[18] However, a federal branch or agency of a foreign bank, with prior approval of the Comptroller, may establish and operate additional branches or agencies in its home and/or other states.[19] This may be done on the same terms and conditions and subject to the same limitations and restrictions as apply to the establishment of branches by a national bank, if the principal office of the national bank was located at the same place as the initial federal branch or agency.[20] Moreover, a foreign bank may establish a federal branch or agency in any state where it does not already operate a state-licensed branch or agency, and in which the establishment of such branch or agency is not prohibited by state legislation.[21] This insures that in the states where foreign banks are welcomed, they will have the option of a federal or state charter.[22] Foreign banks may also convert their existing state-licensed branches or agencies into federally-licensed branches or agencies.[23]

The IBA imposes one significant restriction on the permissible activities of foreign banks. Specifically, federal branches of a foreign bank may accept domestic as well as foreign deposits only within the foreign bank's home state. Outside that state, the IBA requires the branches of a foreign bank to accept only those deposit types that may be accepted by Edge Act corporations;[24] that is, deposits related

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16. *Id.*
17. 12 U.S.C. § 3103(a) (1978).
18. *Id.* at § 3102(e).
19. *Id.* at § 3102(h).
20. *Id.*
21. *Id.* at § 3102(a). *See also* note 14 *supra.*
22. *See* note 14 *supra.*
23. 12 U.S.C. § 3102 (f) (1978). *See also* note 14 *supra.*
24. Under Section 25(a) of the Federal Reserve Act (the so-called Edge Act), the activities of an Edge Act corporation are restricted to servicing the international financial requirements of U.S.-based clients and overseas customers. Thus, an Edge Act corporation may receive foreign deposits but can receive only domestic demand deposits if they are incidental to or for the purpose of carrying out transactions overseas. 12 U.S.C. § 611(a) (1978).

to international trade and commerce.[25] Limited foreign deposit-taking capabilities (i.e., nonresident deposits) are also granted to federal agencies of foreign banks. Federal agencies are, however, prohibited from accepting domestic deposits, but permitted to maintain credit balances.[26] The IBA offers no precise definition of credit balances; instead, the Comptroller and state authorities are allowed to define them as they wish. Lending activities of foreign banks, however, remain unrestricted by the IBA. Undoubtedly, these are issues where the competition of the dual system can prove to be beneficial.

Implications for Florida's Foreign Banking Legislation

The first area of interest is the legal forms of foreign bank organization recognized by the Florida Statutes. The Statutes explicitly provide for the licensing of foreign bank agencies or representative offices only. Implicitly then, state law prohibits federal branch operations by foreign banks within its borders, and IBA provisions on the establishment of branches outside the home state are of no consequence to Florida.[27]

A foreign bank, on the other hand, regardless of its home state, may establish and operate a federal agency in Florida since this form of organization is recognized by state law. What is not recognized, however, is its federal status, as no provision is made in state law for federally-chartered agencies. One may argue that since Florida law allows interstate activity, such as foreign banks from other states establishing a state agency, no distinction should be drawn between out-of-state agencies and federal agencies. In other words, federal agencies should also be permitted.

Another implication for state law is the recognition by the IBA that a federal agency possesses national bank status. As stated earlier, such agency may operate additional agencies subject to the same limitations and restrictions as are applicable to the establishment of branches by a national bank.[28] Hence, a federal agency located in Dade County, Florida, for example, would be permitted to open two additional offices in the county each year whereas a state-licensed agency would be permitted only one.

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25. 12 U.S.C. § 3103(a) (1978).
26. *Id.* at § 3102(d).
27. The language of the IBA strengthens this point further when it states that the establishment of a federal branch outside of its home state must be "expressly permitted by the State in which it is to be operated." *Id.* at § 3103(a).
28. *See* text accompanying note 11 *supra*.

With respect to federal agency lending activities, the IBA only states that federal branches and agencies shall have the same authority as national banks would have within the same state. Accordingly, there is no restriction on the federal agency's lending capabilities. The disparity between the federal agency and state agency lending authorities may exert some pressure on those states, such as Florida, which restrict the lending authority of their respective agencies.

As to the deposit-taking activities of federal agencies, the IBA grants limited foreign deposit-taking capabilities to such agencies, unlike the Florida Statutes. The IBA stance, however, coincides with the Florida Statutes in prohibiting domestic deposits and permitting only credit balances. Several of the states and the Comptroller seem willing to promote a liberal definition of credit balances. In fact, this process is expected to evolve even more rapidly than anticipated, through another section of the IBA which revises pertinent legislation on Edge Act corporations. It is expected to spearhead important changes in state law (Florida's included) on the deposit-taking provisions of foreign agencies. Specifically, Section 3.0 subsection (c) of the IBA amends prior legislation and eliminates the requirement that all Edge Act corporation directors be U.S. citizens. In the same section of the IBA, subsection (f), foreign-owned banks are permitted to own Edge Act corporations to more effectively service the international financing requirements of their U.S.-based clients and overseas customers.

What these provisions mean for Florida is that a foreign bank will now have the alternative of establishing in the state, subject to the approval of the Federal Reserve, an Edge Act corporation with no limitation on its foreign deposit-taking activities. This alternative thus offers a foreign bank a broader deposit-base than does an agency, though it entails a capitalization requirement and an associated lending limit.[29] An agency, on the other hand, is a less effective deposit

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29. The lending of national banks and members of the Federal Reserve System is subject to a limitation commonly referred to as the *ten percent rule*. This rule limits the amount of credit extended to any one borrower on an unsecured basis to ten percent of a bank's capital and surplus. This limitation is designed to curb favoritism in the granting of loans while reducing risk through diversification. An Edge Act corporation capitalized with the minimum capital requirement of $2 million would be able to extend a loan to any one borrower not exceeding $200,000—an amount significantly low for international financing either by domestic or international standards.

vehicle but a more efficient lending form, since it has the capital base of its foreign parent bank on which the lending limit is applied.[30] The choice is now open to all foreign banks, although the best solution may be a combination of both vehicles.

The alternatives available to foreign banks afford them the opportunity to circumvent Florida's restrictions on the deposit-taking activities of their agencies. This raises the question of whether the state's interests might be better served by introducing legislation which permits foreign bank agencies to accept foreign deposits. Such legislation would promote the growth of Florida's international banking community and increase its competitiveness vis-à-vis those of other states.

Conclusion

By setting up a coherent federal framework, the IBA enhances the ability of all states to attract foreign bank facilities on an equal footing and without fear of disruption of local markets. Already, state legislation throughout the country differs widely on the powers of foreign banks. Some states ban foreign banking activity altogether while others permit such activity but only within narrow confines. These legislative limitations on foreign bank entry or operation within state borders reflect the attitudes of local competitive concerns, especially with respect to deposit-taking. The IBA, through its liberal stance, leaves the various states free to decide how aggressively they wish to pursue the development and growth of their international business and investment opportunities.

In the case of Florida, given its desire to establish itself in the international commercial and financial circles, it will be essential to introduce specific legislation which will (a) provide banking agencies with foreign deposit-taking capabilities, and (b) extend the lending authority of state agencies so as to bring them into parity with federal agencies. Such legislation is dictated by the need to attract international banks in order to further Florida's commercial and financial image as a Latin American banking center.

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30. One of Florida's requirements for the issuance of an agency license to a foreign banking corporation is that such corporation must demonstrate that the actual value of its assets is at least $25,000,000 in excess of its liabilities. Stated differently, such corporation must have a minimum net worth of $25,000,000. Assuming this to reflect capital and paid-in surplus, the agency's lending limitation to any one borrower would be at least $2,500,000, which is twelve times larger than that of an Edge Act corporation. *See* FLA. STAT. § 659.67(5)(a)(5) (1977).

APPENDIX

TABLE 1

FOREIGN BANKS OPERATING IN FLORIDA AS OF YEAR-END 1978

Foreign Banks	Status
1. Banco de la Provincia de Buenos Aires, Buenos Aires, Argentina	Representative office
2. Banco Real, S.A. Sao Paulo, Brazil	Operating agency
3. Bank Hapoalim, B.M. Tel Aviv, Israel	Operating agency
4. Bank Leumi le-Israel, B.M. Tel Aviv, Israel	Operating agency
5. The Bank of Nova Scotia Toronto, Canada	Operating agency
6. Israel Discount Bank Ltd. Tel Aviv, Israel	Operating agency
7. Lloyds Bank International Ltd. London, England	Operating agency
8. Standard Charter Bank Ltd. London, England	Operating agency

SOURCE: Division of Banking, Office of Comptroller, State of Florida, Tallahassee.

TABLE 2

FOREIGN BANK APPLICATIONS APPROVED OR PENDING APPROVAL AT YEAR-END 1978

Foreign Banks	Status
Banco de Estado de Sao Paulo, S.A. Sao Paulo, Brazil	Approved agency
Banco de la Nacion Argentina Buenos Aires, Argentina	Approved agency
Banco de Santander, S.A. Santander, Spain	Approved agency
Banco Exterior de Espana Madrid, Spain	Pending approval for agency

SOURCE: Division of Banking, Office of Comptroller, State of Florida, Tallahassee.