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INTERNATIONAL BANKING AND FINANCE

The Securities Activities of Foreign Banks in the United States: A Consideration of Proposed Changes in Regulation

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I. INTRODUCTION

In the past ten years there have been numerous proposals for regulating foreign bank activities in the United States at the federal level. Four bills introduced in 1967,¹ one in 1969,² three in 1973,³ and one in 1974⁴ generated controversy and speculation, but none were reported out of committee. Hearings were held on two of the five bills submitted in the 94th Congress.⁵ H.R. 13,876, the International Banking Act of 1976, passed in the House but not in the Senate in 1976.⁶ It has been resubmitted in the 95th Congress as the International Banking Act of 1977.⁷

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1. H.R. 570, 90th Cong., 1st Sess. (1967) (introduced by Rep. Fine); H.R. 6856, 90th Cong., 1st Sess. (1967) (introduced by Rep. Patman); S. 1741, 90th Cong., 1st Sess. (1967) (introduced by Senators Javits, Brooke, Scott (Pa.), and Kennedy (N.Y.)); H.R. 9867, 90th Cong., 1st Sess. (1967) (introduced by Rep. Gonzalez).

The first three were the result of a 1966 study by Dr. Jack Zwick of Columbia University. See J. Zwick, Joint Economic Committee Paper No. 9: Foreign Banking in the United States, 89th Cong., 2d Sess., 1 (1966).

2. H.R. 4841, 91st Cong., 1st Sess. (1969) (introduced by Rep. Patman).

3. H.R. 11,440, 93d Cong., 1st Sess. (1973) (introduced by Rep. Patman); H.R. 11,597, 93d Cong., 1st Sess. (1973) (introduced by Rep. Rees; this was the Federal Reserve Board's proposal); H.R. 11,690, 93d Cong., 1st Sess. (1973) (introduced by Rep. Dent).

4. S. 4205, 93d Cong., 2d Sess. (1974) (introduced by Senators Sparkman, Tower, McIntyre, and Stevenson).

5. H.R. 5619, 94th Cong., 1st Sess. (1975) (introduced by Rep. St. Germain); S. 958, 94th Cong., 1st Sess. (1975) (introduced by Senators Proxmire, Tower, McIntyre and Stevenson) (Foreign Bank Act of 1975); H.R. 12,103, 94th Cong., 2d Sess. (1976) (introduced by Rep. Reuss); H.R. 13,211, 94th Cong., 2d Sess. (1976) (introduced by Reps. Rees, Reuss, and St. Germain); H.R. 13,876, 94th Cong., 2d Sess. (1976) (introduced by Reps. Reuss, Annunzio, et al). S. 985 and H.R. 5617 were Federal Reserve Board proposals.

Hearings in the Senate were held on S. 958 on Jan. 28, 1976. Hearings on S. 958 Before the Subcomm. on Financial Institutions of the Committee on Banking, Housing and Urban Affairs, Senate, 94th Cong., 2d Sess. (1976). Hearings on H.R. 13,876 were held in the Senate on Aug. 31, 1976. Hearings on H.R. 13,876 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs, 94th Cong., 2d Sess. (1976).

6. H.R. 13,876 passed in the House, as amended, on July 29, 1976. 122 Cong. Rec. 115 (1976).

7. See Hearings on H.R. 7325 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Finance, and Urban Affairs, 95th Cong., 1st Sess. (1977) [hereinafter cited as 77 Hearings].

The proposed legislation is the natural response to the recent growth of foreign banking in the United States,⁸ as evidenced by "multiplying offices, growing assets, increasing importance, and greater visibility of [the] foreign banks."⁹ The current patchwork regulation, accomplished mostly at the state level, creates a number of competitive inequalities between domestic and foreign banks. Foreign banks have an advantage in some areas; other factors favor domestic banks.¹⁰

At present, foreign banks have a choice of the form of operation they will enter into in the United States. A foreign bank organizing a subsidiary, whether state or federally chartered, must obtain the approval of the Federal Reserve Board under the Bank Holding Company Act (BHCA)¹¹ to become a bank holding company. The subsidiary must be insured by the Federal Deposit Insurance Corporation (FDIC),¹² and is subject to federal examination, supervision, and regulation by the Comptroller of the Currency.¹³ Foreign banks may also, and usually do,¹⁴ choose to establish a

8. The growth of foreign banking here and the expanding role of American banks in international banking are interdependent developments. Professor Lees identifies several factors which have been influential: "the significant involvement of the United States in foreign trade, the importance of this country as a source of loanable funds, the special role of the dollar in international finance, the size and efficiency of American banking institutions, and the highly developed securities market in the United States." Lees, *Foreign Banking in the United States: Growth and Regulatory Issues*, 5 Den. J Int'l L. & Pol'y 463, 463-64 (1975) [hereinafter cited as Lees].

9. Welsh, *The Case for Federal Regulation of Foreign Bank Operations in the United States*, Colum. J. World Bus. 98, 98 (Winter 1975).

The Committee Report on H.R. 13,876 states that "[f]ederal regulation is needed in view of the impact of foreign banking institutions on domestic financial markets and the domestic and foreign commerce of the United States, and because most foreign banks operate in the United States in more than one state." H.R. Rep. No. 94-1193, 94th Cong., 2d Sess. 122, 123 (1976).

10. Foreign banks were found to have "five major advantages" in the FINE study of 1975. They are: (1) Through subsidiaries and affiliates, they may underwrite and deal in corporate securities; (2) they can engage in full service banking operations in more than one state, a privilege denied domestic banks under the McFadden Act; (3) they can hold equity investment in U.S. commercial companies or subsidiaries thereof, which U.S. banks and bank holding companies are forbidden from doing; (4) foreign banks are not subject to the "closely related to banking" restriction of the Bank Holding Company Act; and (5) foreign bank branches and agencies escape the restrictions of federal reserve requirements. See Fine, *Financial Institutions and the Nations Economy*, House Comm. on Banking Currency and Housing, 94th Cong., 1st Sess. (1975).

11. Bank Holding Company Act of 1956, 12 U.S.C. § 1841-1849 (1956) (as amended 1970) [hereinafter cited as BHCA].

12. 12 U.S.C. §1842 (e) (1970).

13. 12 U.S.C. § 1817-1829; 1844 (1956) (amended 1970).

14. Most foreign banks do not establish U.S. subsidiaries because of the National Bank Act requirement that all national bank directors be U.S. citizens. 12 U.S.C. § 72 (1956).

branch, agency,¹⁵ representative office,¹⁶ or investment company¹⁷ in the United States. Under existing law, regulation of these forms is left to the States.

Much of the current controversy centers around a facet of federal banking law which has not been applied to foreign banks doing business in the United States: the separation of investment banking functions from commercial banking functions. This wall was erected by the Banking Act of 1933 (Glass-Steagall Act),¹⁸ and has been extended to bank holding companies by Federal Reserve Board rulings under the BHCA.¹⁹ It would be applicable to foreign banks' U.S. subsidiaries, were any to be formed,²⁰ but not to branches, agencies, investment companies, or representative offices, since the latter are not "banks" within the meaning of the Glass-Steagall Act of the BHCA.

The effect of all the proposed statutes would be to force the separation of commercial and investment banking functions,²¹ as envisioned by the Glass-Steagall Act and extended by the BHCA regulations, to all subsidiaries, branches, and agencies of foreign banks. This paper will focus on the appropriateness of that result. It will consider the history of the Glass-Steagall Act and its import for foreign banks, and additional factors which militate either for or against the extension of the Glass-Steagall scheme to foreign banks. It will deal with the scope of the Glass-Steagall Act as currently interpreted as one facet of the foreign bank problem, but it will not attempt a review of the continued desirability of the Glass-Steagall Act. There is no attempt to discuss any other aspect of federal foreign bank regulation.

II. HISTORY AND POLICIES BEHIND THE GLASS-STEAGALL ACT

The pre-Civil War banking system in the United States was modeled after the British financial system, with a "sharp division" between commercial

15. Branches are offices of institutions organized under foreign law. Agencies do not accept deposits. See Edwards & Zwick, *Activities and Regulatory Issues: Foreign Banks in the United States*, 10 Colum. J. World Bus. 58, 65 (Spring 1975).

16. A representative office does not require licensing and is not regulated by the state, but it may not do banking business. It plays a liaison role in developing business contacts for the overseas bank. See Nevans, *The Regulatory Environment: Killing the Golden Goose?*, *Euromoney*, June 1977, at 51 [hereinafter cited as Nevans].

17. New York alone permits investment companies. See N.Y. Banking Law § 507-520 (McKinney 1977).

18. Banking Act of 1933, ch. 89, 48 Stat. 162 (codified in scattered sections of 2, 3, 6, 12 U.S.C.) (1971).

19. 12 C.F.R. § 225.4.

20. See note 14 *supra*.

21. Various methods of effecting the separation have been proposed. One solution would redefine foreign banks' branches and agencies as banks within the meaning of the BHCA. Another would authorize the Comptroller of the Currency to charter federal branches and agencies of foreign banks. The text of section 8 of the International Banking Act of 1977, which would separate commercial and investment banking, is reprinted in the appendix.

banking and investment banking.²² In this vein, the National Bank Act of 1864²³ was construed restrictively to preclude the national banks from underwriting or dealing in most forms of securities.²⁴

The post-Civil War trust companies,²⁵ which could undertake virtually any type of financial activity because they were chartered under state incorporation law, led to broader grants of power for the state-chartered banks.²⁶ The national banks responded by chartering securities affiliates under state law to engage in activities from which the national banks themselves were prohibited.²⁷

22. Perkins, *The Divorce of Commercial and Investment Banking: a History*, 88 *Banking L.J.* 483, 485 (1971) [hereinafter cited as Perkins]. The system on the continent was evolving in a more unified manner, which survives to the present. *Id.* at 485-86. *See also* text at notes 76 & 77 *infra*.

23. 13 Stat. 99, Ch. 106, Sec. 8 (1968). National banks were granted: all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidence of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this title.

Id.

24. Early case law prohibited bank investment in securities except as security for loans. *National Bank v. Case*, 99 U.S. 628 (1878); or when acquired to settle a pre-existing debt. *First Nat'l Bank of Charlotte v. Nat'l Exchange Bank*, 92 U.S. 122, 128 (1875).

An exception was also made for securities of government entities. *See First Nat'l Bank v. Bennington*, 16 Blatchford 53 (N.Y. 1879); *Newport Nat'l Bank v. Board of Education of Newport*, 70 S.W. 186 (Ky. 1902).

Eventually, courts interpreted the National Bank Act as authorizing national banks to invest in state, municipal, and corporate bonds and to participate in bond flotations. *See Dep't of the Treasury, Public Policy Aspects of Bank Securities Activities: An Issues Paper*, (1975), reprinted in *Hearings on H.R. 13,876, Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs, 94th Cong., 2d Sess. (1976)* [hereinafter cited as *Treasury Issues Paper*]. *See also* W.N. Peach, *The Securities Affiliates of National Banks* (1941) [hereinafter cited as *Peach*].

25. Although the trust companies at first concentrated on estates and wills, they eventually accepted deposits as well. Perkins at 487. They also prepared and distributed corporate securities, either for customers or for their own account. *See* F. Redlich, *The Molding of American Banking: Men and Ideas*, 394 (2d ed. 1968).

For a review of the growth of the trust companies and the type of commercial banking activities they undertook, *see* Kazakevich, *Development of Fiduciary Banking*, in H.P. Willis & Chapman, *The Banking Situation* 206, 207-15 (1934).

26. By 1900, state chartered banks had virtually the same powers as trust companies. Perkins, *supra* note 21, at 489. *See generally* Barnett, *State Banks and Trust Companies Since the Passage of the National Banking Act* (1911).

27. Peach *supra* note 24, at 53, 62-66. An excellent discussion of the factors which contributed to the entrance of national banks into the securities business is found in Peach at 16-37.

Affiliates were formed in several ways: (1) Stock in the affiliate was issued to and held by trustees who were bank officers; (2) bank stockholders were given stock in the affiliate, which was then deposited in a trust company; (3) stockholders held shares of the bank and the affiliate; (4) the stock of one affiliate was held by another affiliate; (5) stock of the affiliate was carried as a bank investment; and (6) the affiliate was owned by a holding company which also controlled the parent bank. Peach at 66-70; *see also* *Treasury Issues Paper* at 66, n.15.

Restrictions on the powers of national banks are discussed in note 24 *supra*.

The distribution of World War I war bonds by the national banks²⁸ brought them greater expertise in securities dealings, and gave investors more confidence in securities.²⁹ The Federal Reserve Board tacitly approved the investment operations of state banks and investment companies by admitting both to the Federal Reserve System complete with their securities operations.³⁰

When corporations turned to the securities markets rather than to commercial loans to finance their post-War expansion,³¹ the national banks found it necessary to continue underwriting securities in order to compete with the state banks.³² The McFadden Act,³³ passed in 1926, reaffirmed the power of the national banks to underwrite certain investment securities.³⁴

28. State banks, trust companies, and private bankers also participated in the distribution of government securities during the War.

29. As Peach explains:

Although national banks received no immediate pecuniary reward for their efforts, they benefited indirectly. For not only did they become familiar with the technique of distributing securities, but they gained many contacts with investors and won their confidence, partly because of their patriotic mission, partly because they offered bonds of unquestioned soundness. Individuals, formerly prejudiced against all types of securities, became security minded and potential customers for future issues of corporate securities.

Peach, *supra* note 24, at 32-33, cited in Treasury Issues Paper, *supra* note 24, at 67 app.

30. Perkins, *supra* note 22, at 491, citing C.S. Tippetts, State Banks and the Federal Reserve System 109-12 (1929). The Federal Reserve Act, which created the Federal Reserve System, was passed in 1913.

31. The reasons for the shift from financing through commercial loans to financing in the securities market are detailed in May, *Banks and the Securities Market*, in H.P. Willis & Chapman, *The Banking Situation* 610-33 (1934).

32. Treasury Issues Paper, *supra* note 24, at 68. The Comptroller of the Currency, recognizing the threat to the viability of the national banking system posed by the dominance of the state banks and trust companies, refrained from enforcing the existing restrictions on the national banks' powers. Peach, *supra* note 24, at 50.

The Comptroller's major concern was that the national banks, if too restricted, would reincorporate as state banks, with a resulting loss of the Federal Reserve Board's control over commercial credit. See Annual Report of the Comptroller of the Currency, especially at 2-3 (1926).

33. 12 U.S.C. §§ 24, 29, 34a, 36, 51, 52, 57, 72, 76, 81, 82, 84, 161, 321, 341, 371, 501, 521, 559, 593 (1971).

Representative McFadden found the "authority (for securities affiliates) [in] Section 5136 (Federal Reserve Act) . . . empowering national banks to negotiate 'other evidences of debt . . .'" Hearings on the Consolidation of National Banking Associations Before the Senate Banking and Currency Committee, S. 1732, 69th Cong., 1st Sess. (1926) (statement of Representative McFadden).

Senator Glass, who was to draft part of the Banking Act of 1933, was skeptical: "There is nothing in the National Banking Act that permits it. We . . . [are] being asked to legalize something that has been done without authority of law." Hearings Before the Senate Banking and Currency Committee, S. 3316, 68th Cong., 2d Sess. at 111 (1925), also cited in Perkins, *supra* note 21, at 495.

34. According to the Treasury Issues Paper, "[t]he bill was purposely couched in terms of reaffirming the authority of national banks under preexisting law to engage in the underwriting of securities, rather than granting a new power." H. Rep. 83, 69th Cong., 1st Sess. 2 (1926), cited in Treasury Issues Paper, *supra* note 24, at 69.

The Comptroller of the Currency, given the responsibility for determining what securities could be underwritten by the banks, initially confined approval to debt securities, but eventually approved the underwriting of equity securities as well. Treasury Issues Paper, *supra* note 24, at 70.

That sanction, combined with sharp rises in the stock market from 1927 to 1929,³⁵ stimulated more investment banking activities by commercial banks, so that "by the end of the 1920's the commercial banks, both state and national, [were] the dominant force in the investment banking field."³⁶

The passage of the Banking Act of 1933 (Glass-Steagall Act)³⁷ into law was the result of a combination of factors.³⁸ The crash of 1929 and the subsequent collapse of the banking system were widely attributed to the securities affiliates.³⁹ Egregious abuses of power by banks and bankers, often involving the affiliates, were exposed in the Congressional Hearings of 1931 and 1932.⁴⁰ There was strong support in Congress for the theoretical desirability of separating investment and commercial banking.⁴¹ Other

35. Perkins, *supra* note 21, at 495.

36. Treasury Issues Paper, *supra* note 24, at 70. For an explanation of the underlying causes of the changes in banking structure, control and portfolios, see Willis, *Industrial Changes in Banking*, in H.P. Willis & Chapman, *The Banking Situation* 634-52 (1934).

37. The Act takes its name from Senator Glass, whose bill separated commercial and investment banking, and Representative Steagall, whose proposal led to the formation of the Federal Deposit Insurance Corporation.

38. See generally S.E. Kennedy, *The Banking Crisis of 1933* (1973).

39. See, e.g., the remarks of Representative Fish during hearing on the Glass bill:

There is nothing new about this depression, as far as the principle involved. It is exactly the same as any other. There was an enormous inflation brought about as any other. There was an enormous inflation brought about because of the mass-overproduction of stocks, bonds and other securities largely emanating from these [bank security] affiliates, which were sold to the American people often without much investigation, and as a result it meant a mass over production of factories, commodities, real estate, and everything else — and enormous inflation that sooner or later had to crash and when it did crash and the pendulum swung back, it did not stop at normalcy but went right on down into the depths where we are now.

77 Cong. Rec. 4028 (1933) (remarks of Rep. Fish).

The failure of the Bank of the United States, whose president had appropriated vast amounts of bank funds for personal speculative business ventures through the bank's securities affiliates, was also attributed to the bank affiliate system. See Perkins, *supra* note 21, at 496-97; *Investment Company Institute v. Camp*, 401 U.S. 617, 629 (1971).

40. Hearings on S. Res. 71, 71st Cong., 3d Sess. (1931); Hearings on S. 4412, 72d Cong., 1st Sess. (1932); Hearings on S. 4115, 72d Cong., 1st Sess. (1932). See also S. Rep. 493, 71st Cong., 2d Sess. (1930); H. Rep. 150, 73d Cong., 1st Sess. (1933); S. Rep. 77, 73d Cong., 1st Sess. (1933); H. Rep. 254, 73d Cong., 1st Sess. (1933).

The Questionnaire on Securities Affiliated employed in the Senate Banking Committee Hearing is reprinted, together with the answers thereto, in Bogen, *The Affiliate System*, in H.P. Willis & Chapman, *The Banking Situation* (1934).

41. Senator Glass and Professor Willis, drafters of the Glass Bill, firmly believed that the proper role of commercial banks was to allocate capital through commercial loans, and not to engage in securities speculation. Perkins, *supra* note 21, at 501. This idea is further explained in the Treasury Issues Paper, *supra* note 24, at 73-76.

The same ideas had previously been advanced in the Pujo Hearings of 1912 and 1913, which were convened to investigate the concentration of money and capital in a "money trust." See Report of the Committee to Investigate the Concentration of Money and Credit, 62d Cong., 3d Sess. (1913).

Most economists today assume that capital is efficiently allocated to businesses through the securities markets. See generally W. Baumol, *The Stock Market and Economic Efficiency* (1965); E. Fama & M. Miller, *Theory of Finance* (1972); but see A. Smith, *The Money Game*, 12, 23, 44-47 (1968).

pending legislation⁴² had captured the attention of much of the financial community.⁴³ In 1933, the revelations of the Pecora Committee's investigation into stock exchange practices,⁴⁴ coupled with the national bank moratorium,⁴⁵ provided the final push toward the passage of the Glass-Steagall Act.

Four major policy reasons for the passage of the Glass-Steagall Act can be discerned from the legislative history. First, Congress concluded that the commercial banks' involvement with securities affiliates had undermined their financial viability, and the Glass bill was to aid in maintaining the stability of the commercial banking system, in insuring public confidence in commercial banks, and in protecting investors by preventing a recurrence of previous events.⁴⁶ Second, Congress believed that a complete separation of commercial and investment banking would eliminate any possible conflicts of interest arising from performing both activities.⁴⁷ Third, Congress believed that bank securities operations "tended to exaggerate financial and business fluctuations and undermine the economic stability of the country by diverting bank deposits into 'speculative' securities investments."⁴⁸ Finally, Congress sought to limit the concentration of economic, financial, social, and political power.⁴⁹

The Glass Subcommittee of the Senate Banking and Currency Committee identified a number of specific abuses which it hoped to eliminate through the separation of functions. These included:

(1) Banks supported their securities affiliates by purchasing securities from them, either for their own account or for accounts handled in a fiduciary capacity, to relieve the affiliates of excess holdings or to assure the success of a particular underwriting venture.⁵⁰

(2) Large banks promoted their securities business by distributing securities underwritten by their affiliates to regional correspondents which relied on them for investment advice.⁵¹

42. Both the proposal establishing the Federal Deposit Insurance Corporation and the Securities Act of 1933 were pending. The latter protects investors against abuses from false or misleading information in connection with securities underwritings, a common practice in the late 1920's.

43. Treasury Issues Paper, *supra* note 24, at 83 app.

44. See Hearings to Investigate Practices of Stock Exchanges Before the Senate Banking and Currency Committee, 72d Cong., 1st Sess. (1933); Hearings on S. Res. 84, 72d Cong., 2d Sess. (1933).

Kennedy summarizes the Pecora Hearings. S.E. Kennedy, *The Banking Crisis of 1933*, at 103-28 (1973).

45. For a discussion of the events surrounding the banking moratorium, see H.P. Willis & Chapman, *The Banking Situation*, 21-29 (1934).

46. Treasury Issues Paper, *supra* note 24, at 27-28.

47. *Id.*

48. *Id.* See also 77 Hearings, *supra* note 7, at 216-17 (Securities Industry Ass'n Memorandum for Study and Discussion on Bank Securities Activities) [hereinafter cited as SIA Memo].

49. SIA Memo, *supra* note 48, at 216.

50. Treasury Issues Paper, *supra* note 24, at 80 app.

51. *Id.*

(3) Bank loans were used to advance the operations of the securities affiliates. Banks could (a) lend directly to the affiliates to finance underwriting, (b) lend to customers for the purchase of securities underwritten by their affiliates, or (c) lend to corporations which used the banks' affiliates to underwrite their securities issues.⁵² Such loans were often granted, but not as a result of objective business decisions. Banks often failed to require adequate collateral, or overvalued securities given them as collateral for loans.⁵³

(4) Banks could and did make unwise investments, knowing that they could be concealed by being shifted to the securities affiliate, thereby removing them from the banks' condition statements.⁵⁴

(5) Affiliates could manipulate the price of the parent banks' stock by dealings in the market. Affiliates could also push the sale of the banks' stock to depositors.⁵⁵

(6) Insider-dealing by bank officers and directors was prevalent, and the misuse of the securities affiliates was frequently very profitable.⁵⁶

There were also many abuses not related to the securities affiliates which the Glass-Steagall Act was not meant to cover.

III. IMPLICATIONS OF THE HISTORY AND POLICIES BEHIND THE GLASS—STEAGALL ACT FOR FOREIGN BANK REGULATION

In evaluating the applicability of the Glass-Steagall Act to foreign banks, there are three relevant questions: (1) Are foreign banks any more or less susceptible than domestic banks to the abuses which Congress sought to eliminate? (2) would the separation of commercial and investment banking functions of foreign banks further the general policies which Congress sought to implement? and (3) what other considerations bear on the problem?

There has been very little consideration of the question of possible abuses,⁵⁷ because there is little evidence to suggest that foreign banks are any more, or less, likely to abuse their securities affiliates than domestic banks.⁵⁸ The only possible basis of difference is the variation in the regulatory climate of the parent bank. In many of the countries whose banks have established securities affiliates in the United States, "universal"

52. *Id.*

53. *Id.* at 81.

54. *Id.* at 82.

55. *Id.*

56. *Id.*

57. Those who favor regulation tend to state without further analysis that the legislative history of the Glass-Steagall Act and the BHCA indicate that Congress believed the combination of investment and commercial banking would cause "serious economic problems." Opponents of foreign bank legislation are prone to ignore the question of possible abuses and focus on the general policies, where they have a better slant.

58. "Abuses envisioned in the BHCA and Glass-Steagall Act apply to the operations of foreign bank branches and agencies as well as to the operations of domestic banks. For example, branches and agencies could lend to a U.S. commercial entity in which their parent had a controlling equity interest at a favorable rate, thus giving such entity an advantage over its U.S. competitors." Welsh, *supra* note 9, at 105.

banking—in which the same bank performs both investment and commercial functions—is the rule.⁵⁹

The exclusion of foreign banks from Glass-Steagall's provisions on the basis of adequate control by the home country, however, would necessitate an examination of each country's banking system, and of decisions made on an individual country basis. Such a solution is not only impractical, but also politically unwise.

Individual treatment based on a country's regulatory climate may contravene the provisions of the United States' many Friendship, Commerce, and Navigation (FCN) treaties and could, therefore, be unconstitutional. Typical FCN treaties require that the nationals and companies of other countries be accorded "most-favored-nation treatment."⁶⁰ "Most-favored-nation treatment" means "treatment within the territories of a Party upon terms no less favorable than the treatment accorded therein, in like situations, to nationals and companies . . . of any third country."⁶¹ Such treaties further provide that

[e]ach Party reserves the right to limit the extent to which aliens may establish, acquire interests in, or carry on enterprises engaged within its territories in . . . taking and administering trusts, [and] banking involving depository functions. . . . [N]ew limitations imposed by either Party . . . shall not be applied as against enterprises which are engaged in such activities . . . at the time such new limitations are adopted. . . . Moreover, neither Party shall deny to . . . banking companies of the other Party the right to maintain branches and agencies . . . to perform functions necessary for essentially international operations in which they engage.⁶²

Under these provisions, it appears that the United States may impose limits on those foreign banks whose U.S. operations involve fiduciary or depository functions, but may not prohibit "essentially international" activities. Any regulatory provision would have to be carefully drafted to meet these requirements.

Furthermore, any application of the Glass-Steagall prohibitions to banks of countries whose regulation of their "universal" banking system was considered unsatisfactory, but not to banks of other countries whose self-regulation was considered acceptable, would at least be subject to constitutional attack on the basis of the "most-favored-nation" clause.

59. 77 Hearings, *supra* note 7, at 343 (Statement of E.E.C. Banking Federation) [hereinafter cited as E.E.C. Statement].

60. *See, e.g.*, Treaty of Friendship, Commerce and Navigation, Oct. 29, 1954, United States-Germany, 7 U.S.T. 1839, T.I.A.S. No. 3593.

61. *Id.* at art. XXV, para. 4.

62. *Id.* at art. VI, para. 2.

Ultimately, consideration of the issue of possible abuses is not very useful.⁶³ "Questions of competition, concentration of banking power, conflicts of interests, and soundness of banking operations with which the regulatory policies of the Glass-Steagall Act and BHCA are basically concerned"⁶⁴, must be addressed.

A key argument for exempting foreign banks from the separation scheme is that the Glass-Steagall Act was not designed to regulate such activities of foreign banks which are dissimilar to the practices of domestic banks.⁶⁵ The principal sphere of the commercial activities of foreign banks here involves the financing of foreign trade,⁶⁶ although recently there has been some expansion into retail banking in New York and California⁶⁷ and into the entire range of wholesale banking. The investment business of foreign banks is largely confined to servicing foreign customers in U.S. markets,⁶⁸ traditionally a part of banking business in many home countries. Again, it should be noted that there is a recent trend for affiliates of foreign banks to increase their participation in U.S. corporate underwritings, although "their relative participation is small and has remained almost constant when compared to the aggregate capital raised in the corporate securities markets (only three one-hundredths of one percent)."⁶⁹

To the extent that foreign banks do not accept deposits, one facet of the Congressional desire to encourage the financial viability of banks drops out. Although the protection of depositors is no longer of concern, the goals of insuring public confidence and in maintaining the stability of the entire

63. Paul Volcker, President of the Federal Reserve Bank of New York, comments that "[although] you may conceivably need to prevent abuses, I don't think you can make a case on something that might be called 'abuses' at present." *Paul Volcker puts the case for stricter rules.* Euromoney, June 1977, at 54. [hereinafter cited as Volcker].

64. Welsh, *supra* note 9, at 105.

65. *Id.* at 106.

66. Halperin, *The Regulation of Foreign Banks in the United States*, 9 Int'l Law. 661, 662 (1975) [hereinafter cited as Halperin].

67. *Id.* at 663. Halperin explains:

Foreign Banks have tended to expand their retail operations by merging with or acquiring United States banks which already possess a number of retail branches. . . . Antitrust enforcement efforts directed against domestic bank mergers have facilitated the entry of international banks into American markets.

The expansion into retail banking has provoked the most heated opposition from small and medium sized independent banks who are facing increasingly aggressive competition from foreign banks bidding for consumer business.

68. Welsh, *supra* note 9, at 104; 77 Hearings, *supra* note 7, at 302-03 (statement of John F. Lee, Executive Vice President, New York Clearing House Association) [hereinafter cited as N.Y. Clearing House Statement].

69. Hearings on S.958 Foreign Bank Act of 1975, Before the Subcomm. on Financial Institutions of the Senate Committee on Banking, Housing, Urban Affairs, 94th Cong., 2d Sess., 233 (1976) (statement of George H. Dixon, Deputy Secretary of Treasury).

commercial banking system are still applicable.⁷⁰ Again, to the extent that foreign funds rather than domestic funds are diverted into the "speculative" securities investments, there is less reason to worry about the effects of that movement of capital on the local economy. However, as world financial markets become increasingly integrated, that argument will gradually become less cogent.

Concern for the concentration of economic, financial, social, and political power should be relegated to federal control, whether it be regulatory or permissive. The current lack of federal policy leaves regulation up to those states which have decided to allow foreign banks to do business within their borders. As Welsh points out, "a national, not state, perspective is required to assess the affiliations of foreign banks of securities. . . firms, since the latter are not subject to state banking boundaries."⁷¹ The United States is "virtually the only [country] in the world in where [*sic*] neither the central government nor the central bank, has a say in the regulation of foreign banks."⁷²

The analytical difficulty in attempting to apply the policies Congress sought to implement in 1933 is that the current situation is confronted by "facts clearly not then contemplated by Congress."⁷³ This 45 year difference demands the careful consideration of other relevant factors in addition to historical policy analysis.

IV. ADDITIONAL FACTORS

The most commonly advanced reason for extending the separation of commercial and investment banking to foreign banks operating locally is that domestic and foreign banks should receive equal treatment under the law.

Proponents of equality as a basis for federal regulation advance two lines of argument to support their position. The first contends that parity of treatment is theoretically desirable; the second attacks the unequal treatment of domestic and foreign banks because of the establishment of an intolerable competitive advantage for foreign banks over domestic banks.

70. Welsh elucidates:

While branches and agencies have small domestic deposit-taking activities, they do play significant roles in international trade financing, commercial lending, and foreign exchange and money-market operations. Should a branch or agency of a foreign bank in this country have to close its doors, it would not only affect depositors (at a branch) but also other U.S. creditors of the branch or agency, including specifically many domestic banks, and would undoubtedly have an effect on the nation's financial markets. Given the multistate operations of many foreign banks, these effects could be felt throughout the country.

Welsh, *supra* note 9, at 107.

71. Welsh, *supra* note 9, at 105.

Another justification offered for establishing federal policy is the problem of effectively controlling the money supply. Halperin argues that "foreign bank offices in the United States can shift funds in and out of the country using overseas sources which are unresponsive to United States policies." Halperin, *supra* note 66, at 671; See also Volcker, *supra* note 63, at 56.

72. Terzakis, *How to Regulate Foreign Banks?*, 68 *Banking* 72, 74 (1976).

73. SIA Memo, *supra* note 48, at 217.

Many advocates of equal treatment base their position on principle rather than on the existence of actual harm: "It is a cardinal principle of United States policy that foreign companies operating in this country should be subject to the same rules and regulations which govern domestically owned companies."⁷⁴ These commentators recognize that while foreign banks enjoy certain competitive advantages over domestic banks, they are also subject to some restrictions which do not apply to domestic banks.⁷⁵ In this vein, any regulation of foreign banks should remove both competitive advantages and handicaps.

Opponents of regulation assert that, regardless of the desirability of equal treatment, it is impossible to achieve. They contend that because of the different structure of investment and commercial banking systems in foreign banks' home countries, what purports to be equal treatment will, in fact, be unequal treatment in some cases.

In continental Europe, for example, a "universal" banking system which integrates commercial and investment banking is common.⁷⁶ Banks act as depository institutions as well as buyers and sellers of shares in industrial and commercial enterprises. The governments of countries on the continent have, at times, requested banks to purchase securities; on other occasions, economic necessity has forced the banks to acquire commercial and industrial holdings in order to sustain certain enterprises.⁷⁷ Applying the Glass-Steagall Act's restrictions to U.S. affiliates of such universal banks would force them to choose between establishing commercial banking operations here or extending their securities operations, which are a normal part of their business, to the United States.⁷⁸ This scheme curtails entry into the U.S. market by banks from countries with an integrated system, while giving countries with systems similar to ours full access. Countries with an integrated system are disadvantaged in the United States simply because their banking system has evolved differently. The end result is "equal" treatment between U.S. and foreign banks at the expense of unequal and discriminatory treatment of foreign countries. Whether this is unfair or undesirable is ultimately a question of policy.

74. Halperin, *supra* note 66, at 661.

75. *E.g.*, the requirement that directors of Federal Reserve Banks be U.S. citizens, *supra* note 14, and the limitations on access to the Fed's discount window.

76. E.E.C. Statement, *supra* note 59, at 343.

77. 77 Hearings, *supra* note 7, at 338-39 (statement of Dr. Wolfgang Jang).

78. The E.E.C. contends that extension of the Glass-Steagall Act to foreign banks would "close the door to new continental European securities operations in the United States because no one else but banks are in the securities business in most European countries." E.E.C. Statement, *supra* note 59, at 345.

The E.E.C. statement points out that

[t]hese [European] banks are not asking that the American unit of a European bank be allowed to perform both commercial and securities activities within the United States. They ask only that the foreign banks not be prohibited from establishing two *separate units* in the United States, one to perform commercial banking activities and the other, investment banking activities, solely because outside the U.S., in their home country, the parent banks perform both functions [emphasis added].

Id. at 344.

The situation is complicated by the fact that U. S. banks are allowed to engage in securities operations abroad through Edge Act corporations, despite the illegality of such activities here. We allow our own banks to take advantage of the differences in banking systems abroad, while curtailing the activities of foreign banks in this country to fit the U. S. system.⁷⁹ Thus, the practical result of applying the separation principle would be to "give free reign to U.S. banks and securities firms to compete very strongly in Europe in all areas while telling European banks they would be allowed to compete in only one or the other area."⁸⁰ This is logically consistent in terms of reciprocity; in both cases foreign banks are accorded the same treatment that domestic banks in that country would receive.

There are, however, weaknesses with the reciprocity argument. A key problem is that "the nationality of banks has little bearing on the questions of competition, concentration of banking power, conflicts of interests, and soundness of banking operations with which the regulatory policies of the Glass-Steagall Act and BHCA are basically concerned."⁸¹ An additional problem is that reciprocity "results in banking institutions coming from different banking traditions and environments operating under different sets of rules in the United States," a policy which could be "both politically and economically unsatisfactory."⁸² What seems at first blush to be a logical principle should probably be rejected for the foregoing reasons, although this, again, is a question of policy.

As to the second line of reasoning, the focus is usually on the "unfair competitive advantage" of foreign banks which have both securities companies and commercial banking operations in the United States. Foreign banks are able to offer their customers the entire spectrum of banking services while American banks must choose between investment and commercial banking. Ironically, those U.S. banks which have commented on the proposed legislation do not favor it; rather, they believe that the resulting increase in activity in large U.S. cities is to their benefit.⁸³

A second facet of the unfair competition argument concerns the special privileges granted to banks because of their importance as financial intermediaries. Banks receive favorable tax treatment. In addition, banks benefit from the entry restrictions. They are able to obtain funds at comparatively low rates from depositors, from other banks in the federal funds market,

79. 77 Hearings, *supra* note 7, at 394-95 (statement of James E. David, President of the Boston Stock Exchange, Inc.) [hereinafter cited as Boston Stock Exchange Statement].

80. French Bankers Association deputy managing director Paul Fabre, quoted in Hendrickson, *Foreign Banking in America II: Will Congress Finally Crack Down on Foreign Banks?*, Inst. Investor, Sept. 1977 at 137, 138.

81. Welsh, *supra* note 9, at 105.

82. *Id.*

83. "We're in favour of competition. The more entrants, the better the game, says George Sharp of Citibank. 'New York's foreign exchange business is more important now because these large foreign banks are here. It lends credibility to New York as a foreign exchange center. And the foreign banks have brought with them a greater demand for sophisticated banking deals, which used to be found only in London, Paris, or Hong Kong.' "

Nevans, *supra* note 16, at 23.

and at the Federal Reserve discount window. The securities industry argues that these privileges, which are ultimately paid for by the taxpayer or the depositor, are intended to make low cost credit available and should not be used to benefit banks' non-banking activities — more specifically, their securities activities.⁸⁴ The gist of the argument is that U.S. broker/dealers cannot compete with foreign banks' securities affiliates because of the special advantages garnered by the latter in their role as banks.

Some of these advantages, however, are limited to domestic banks.⁸⁵ Further, to the extent that foreign banks' securities affiliates focus on non-domestic underwriting,⁸⁶ they do not compete with most domestic broker-dealers.⁸⁷ The major flaw in the securities industry's argument is that it can also be applied to the securities activities currently performed by domestic commercial banks.

There are undeniable advantages. Two questions come to mind: (1) How important is it that foreign banks be able to provide the full range of banking services in light of the securities activities which U.S. commercial banks currently perform and (2) how important are the differences between foreign securities affiliates and domestic securities firms, and between foreign banks and domestic commercial banks, given the relatively small scope of all foreign banking operations in the United States?

The scope of securities operations of U.S. commercial banks has increased enormously since World War II. Banks currently engage in five major types of securities activities, either directly or through affiliates performing "bank-related activities," as permitted by the BHCA. The areas are (1) Agency or brokerage-oriented services; (2) money management services; (3) financial advisory work; (4) medium and long-term lending and private placement services; and (5) investment banking activities abroad.⁸⁸ These activities are described in greater depth in the Appendix.

Despite the encroachments on traditional investment banking activities,⁸⁹ there remain some areas into which commercial banks have either chosen not to enter, or are prohibited from entering.⁹⁰ The Glass-Steagall Act prohibits the flotation, issue, underwriting, public sale, or distribution

84. SIA Memo, *supra* note 48, at 217.

85. See notes 14 and 74, *supra*.

86. Cf. text accompanying notes 66-69 *supra*.

87. Lees believes that "[f]rom a practical standpoint foreign banks are not an important factor in the securities or investment banking industry in the United States." Lees, *supra* note 8, at 474.

88. The first four categories are suggested by the Treasury Issues Paper, *supra* note 24.

89. SIA Memo, *supra* note 48, at 220.

90. Section 16 of the Glass-Steagall Act expressly limits dealing in securities by national banks to "purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the [national bank] shall not underwrite any issue of securities or stock." 12 U.S.C. § 24 (1971).

Section 21 of Glass-Steagall Act, which bars any person or organization engaged in underwriting securities from engaging at the same time to any extent whatever in the business of deposit banking, in effect extends the securities prohibitions to insured nonmember banks. 12 U.S.C. § 378(a) (1971).

corporate securities,⁹¹ the underwriting of municipal revenue bonds (with a few limited exceptions),⁹² and the sponsorship of open-end investment companies or mutual funds. To date, commercial banks have not gone into the retail brokerage business, although it is unclear whether the relevant statutory language actually prohibits them from doing so.⁹³ Banks do act as liaisons between customers and broker/dealer firms.

By far the most important activities from which commercial banks abstain are the dealings in corporate securities, previously discussed. In evaluating how much of a handicap this is, it is instructive to note who is complaining about it. Much of the opposition to the proposed legislation has come from foreign banks, regional stock exchanges, and large New York banks. The Securities Industry Association and the Bankers for Foreign Trade (representing regional banks) have favored the proposed statute.

The positions of the regional stock exchanges and the Securities Industry Association are based on fears of decreased business. The regional exchanges want to continue to reap the benefits that foreign brokerage firms bring to them,⁹⁴ while the securities industry opposes the activities of either domestic or foreign banks in the securities market.⁹⁵ The big New York banks feel they have much in common with the foreign banks,⁹⁶ and do not want restrictive legislation while review of the Glass-Steagall Act is pending.

The regional banks favor extension of the Glass-Steagall separation because they object to competition in the retail banking area.⁹⁷ Few regional and state banks have any interest in entering the securities arena.

In all, the banks which stand to be hurt by the current permissive policy are not asking for relief from that policy. It is other, often more general, interests that have expressed strong feelings. The fair implication from this is that foreign banks' securities affiliates do not now have a very significant competitive advantage, although concededly that could change.⁹⁸

The growth of foreign banking has had positive implications in many money-related areas. The influx of foreign bank operations "has immeasurably enhanced New York's role as an international financial center and greatly added to the international character of what not so long ago was primarily a domestic market. Similarly, the move of foreign banks to California has substantially contributed to the international orientation of

91. 12 U.S.C. § 24 (1971).

92. See 12 C.F.R. § 1.3(g) (1977).

93. Treasury Issues Paper, *supra* note 24, at 36.

94. See text accompanying note 103, *infra*.

95. See, e.g., 77 Hearings, *supra* note 7, at 209 (statement of Edward I. O'Brien, President, Securities Industry Association).

96. See the strong opposition to H.R. 7325 by the New York Clearing House Association, which has as members most of New York's major commercial banks. New York Clearing House Statement, *supra* note 68, at 295-96.

97. Note 67 *supra*.

98. See Edwards & Zwick, *Activities and Regulatory Issues: Foreign Banks in the United States*, 10 Colum. J. World Bus. 58, 66 (1975) [hereinafter cited as Edwards & Zwick].

banking in that state.”⁹⁹ There is greater breadth and depth in the U.S. money market and foreign exchange market, and better service for multinational corporations and foreign-traders who require international financing.¹⁰⁰ More specifically, the foreign banks’ securities operations have contributed to the growth of the U.S. economy as well as to the world economy. Both direct and portfolio investments here, by corporations and by individuals, have been facilitated by the foreign securities affiliates.¹⁰¹

The regional stock exchanges of which European banks’ securities affiliates are members are especially interested in preventing the split of foreign banks’ commercial and investment banking.¹⁰² Foreign member-firms provide a “wide range of services . . . to both domestic and foreign investors,” the most important of which are: (1) As dealer specialists on the regional exchanges, and (2) as dealers for their own accounts and risk in international arbitrage. Both of those activities will be banned by separationist legislation.¹⁰³ The thrust of the regional exchanges’ argument is that separation runs contrary to the principle of fostering competition among market centers,¹⁰⁴ one of the prime purposes of the 1975 Amendments to the Securities Acts. The open membership provided by the Amendments may be denied only if minimum capital or competency requirements are not met, or by statutory disqualification. The House Commerce Committee and the Senate Banking Committee which considered the amendments made a conscious decision not to prohibit securities affiliates of foreign banks from membership.¹⁰⁵ The exchanges argue that it would be “inconsistent for Congress, on the one hand, to prohibit a United States securities exchange from discriminating against a securities firm of foreign bank parentage, and on the other hand, to forbid a securities firm of foreign bank parentage with a commercial banking presence in this country from being a . . . member of a United States stock exchange”¹⁰⁶

Also supporting the status quo is the fact that the foreign banks’ “overall impact on our balance of payments has been favorable.”¹⁰⁷ This is attributable in part to the balances supplied by foreign banks to their agen-

99. Klopstock, *Foreign Banks in the United States: Scope and Growth of Operations*, Fed. Res. Bd. N.Y., Monthly Rev., June 1973, at 140, 150 [hereinafter cited as Klopstock].

100. *Id.* at 153.

101. *Id.*

102. The regional exchanges are affected more than the New York and American Stock Exchanges because the latter have not permitted foreign-controlled firms to become members until very recently, while the regional exchanges have permitted such memberships. 77 Hearings, *supra* note 7, at 89 (Boston Stock Exchange Statement).

103. *Id.* at 388-89.

104. 77 Hearings, *supra* note 7, at 426 (Statement of Michael S. Tobin, President, Midwest Stock Exchange, Inc.).

105. Boston Stock Exchange Statement, *supra* note 79, at 394. This is consistent with the treatment of U.S. banks’ Edge Act affiliates, which are allowed to engage in securities activities in many foreign countries despite the fact that Edge Act affiliates securities would not be legal here; while foreign banks’ securities affiliates operations are sanctioned at home. *Id.*

106. *Id.* at 395.

107. Klopstock, *supra* note 99, at 153.

cies and branches to enable them to finance their operations,¹⁰⁸ and in part to the channeling of foreign funds into the U.S. capital market induced by foreign securities affiliates, which convert liquid dollar holdings into non-liquid investments. Although it is "difficult to quantify the net effect of foreign banking on this nation's balance of payments because of a lack of published data, there appears to be a concensus among authorities that the expansion of foreign banks has had a positive, if uncontrolled, impact."¹⁰⁹

Many of those who oppose regulation of foreign banks' securities operations do so on the belief that the negative consequences of forcing foreign banks to divorce their commercial and investment banking functions outweigh any reason to take such action.

The fear of retaliation by foreign countries is probably the most frequently advanced argument, but it is often no more than an unsupported slogan. It is a bi-polar issue. Some believe that the proposed regulation "is likely to invite retaliation"¹¹⁰ while others opine that such legislation "should not provide a basis for retaliation by foreign governments."¹¹¹

Most of the response from other countries has not been official criticism but rather reactions from banks, banking organizations, and others who have an interest at stake.¹¹² The German and Swiss governments have, however, "express[ed] uneasiness over certain aspects of the proposed International Banking Act."¹¹³

A "grandfather" clause permitting securities affiliates which were established in good faith reliance on existing U.S. laws to continue their operations would lessen the possibility of retaliation.¹¹⁴ The grandfathering issue, however, has been one of the most hotly contested. Proponents of grandfathering argue fairness, while opponents demand an across-the-board application of the principles of the Glass-Steagall Act. The arguments are much the same as those for and against the extension of the Glass-Steagall Act in the first instance.

The retaliation issue is a touchy one because "[t]he potential loss for the United States is much greater than for foreign banks, and retaliation against U.S. banks would seriously damage U.S. foreign commerce as well

108. *Id.* Both the "initial capital invested by foreign banks to establish offices, [and the] subsequent advances to American affiliates, represent a net inflow of capital." *Id.*

109. Halperin, *supra* note 66, at 671. Other reasons for the net positive effect on the balance of payments are (1) "deposits made by foreigners in United States offices of foreign banks have generally exceeded the volume of foreign loans made by these institutions . . . [and (2)] those foreign banks which have played a major role in trade financing have contributed to improving our trade balances." *Id.*

110. N.Y. Clearing House Statement, *supra* note 68, at 305. See *German Banks Attack Equal Treatment*, *Am. Banker*, July 13, 1976.

111. 77 Hearings, *supra* note 7, at 671 (Statement of Paul H. Boeker, Acting Assistant Secretary for Economic and Business Affairs, Department of State).

112. See Welsh, *supra* note 9, at 102.

113. 77 Hearings, *supra* note 7, at 641 (Statement of Anthony M. Solomon, Under Secretary of the Treasury).

114. See, e.g., 77 Hearings, *supra* note 7, at 649 (Swiss Banks' Policy Position); SIA Memo, *supra* note 48, at 288.

as have an adverse impact on the U.S. economy."¹¹⁵ It is difficult to tell exactly what the chances of retaliation are. It does seem, however, that the problem is not irresolvable, and should not be weighed too heavily against the proposed legislation.

Another objection to federal legislation in this field is the possibility of extraterritorial application of U.S. law. One concern is that the authority of U.S. banking authorities should not be extended to foreign banks' home offices or to regulation of the organization and internal affairs of a foreign bank.¹¹⁶ Another potential problem, the effect on foreign banks' U.S. industrial holdings, falls within the realm of the BHCA.¹¹⁷ As neither of these concerns relate directly to the provisions of the Glass-Steagall Act, the extraterritorial law problem should not be asserted as a stumbling block to the divorce of commercial and investment banking.

V. CONCLUSION

The history and policies behind the Glass-Steagall Act and the pros and cons of extending it to foreign banks are important, but one further factor must be considered: the Congress recently has undertaken a review of the Glass-Steagall Act with respect to domestic banks.¹¹⁸ Many believe that the Glass-Steagall Act is obsolete and redundant in today's world, while others believe that it is necessary for the continued health of the U.S. banking system. Although repeal or amendment of the Glass-Steagall Act does not seem imminent, it is difficult to perceive much rationality in extending a statute, the provisions of which are not entirely clear¹¹⁹ and the vitality of which is questionable.

The importance of the proposed legislation is reflected in the great volume of commentary it has generated. Moreover, the U.S. solution to this problem may set precedent for foreign countries.¹²⁰ There is a need for careful balancing of the various interests at stake.

Clearly, the cost of delay is less than the cost of adopting a "hasty, uninformed remedy."¹²¹ An examination of the policy reasons for separating commercial and investment banking is an appropriate predecessor to federal

115. Perkins, *supra* note 22, at 116. See also Lees, *supra* note 8, at 682.

116. See 77 Hearings, *supra* note 7, at 651 (Swiss Banks' Policy Position).

117. The problem occurs when a foreign bank has a controlling interest in a manufacturer in its home country and that manufacturer has U.S. subsidiaries. Application of the BHCA could result in "a U.S. tail wagging a much larger foreign dog—perhaps contrary to a national directive of a foreign bank's home country." Welsh, *supra* note 9, at 105.

118. See "The Securities Activities of Commercial Banks, Study Outline," Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs, 94th Cong., 1st Sess. (1975); Hearings on the Securities Activities of Commercial Banks Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs, 94th Cong., 1st Sess. (1975) (900 + pp.); Hearings on Brokerage and Related Commercial Bank Activities Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs, 94th Cong., 2d Sess. (1976) (1100 + pp.).

119. See text accompanying note 93 *supra*.

120. See Hutton, *The Regulation of Foreign Banks—A European Viewpoint*, 10 Colum. J. World Bus., 109, 109 (1975).

121. Edwards & Zwick, *supra* note 98, at 66.

foreign bank regulation in this field. "The wisdom and effectiveness of the Glass-Steagall Act in a world of multinational financial markets and institutions is not obvious."¹²²

APPENDIX INTERNATIONAL BANKING ACT OF 1977, SECTION 8

SEC. 8 (a) Except as otherwise provided in this section (1) any foreign bank that maintains a branch or agency in a State, (2) any foreign bank or foreign company controlling a foreign bank that controls a commercial lending company organized under State law, and (3) any company of which any foreign bank or company referred to in (1) and (2) is a subsidiary shall be subject to the provisions of the Bank Holding Company Act of 1956, and to sections 105 and 106 of the Bank Holding Company Act Amendments of 1970 in the same manner and to the same extent that bank holding companies are subject thereto, except that any such foreign bank or company shall not by reason of this subsection be deemed a bank holding company for purposes of section 3 of the Bank Holding Company Act of 1956.

(b) After December 31, 1985, no foreign bank or other company to which subsection (a) applies on the date of enactment of this Act may retain direct or indirect ownership or control of any voting shares of any nonbanking company in the United States that it owned, controlled, or held with power to vote on the date of enactment of this Act or engage in any nonbanking activities in the United States in which it was engaged on such date unless authorized by subsection (c) of this section or by the Board of Governors of the Federal Reserve System under section 4 of the Bank Holding Company Act of 1956.

(c) After December 31, 1985, notwithstanding the prohibitions of subsection (b) of this section, a foreign bank or other company to which subsection (a) applies on the date of enactment of this Act may continue to engage in nonbanking activities in the United States in which directly or through an affiliate it was lawfully engaged on December 3, 1974 (or on a date subsequent to December 3, 1974, in the case of activities carried on as the result of the direct or indirect acquisition, pursuant to a binding written contract entered into on or before December 3, 1974, of another company engaged in such activities at the time of acquisition) and may retain direct or indirect ownership or control of any voting shares of any nonbanking company that it (1) owned, controlled, or held with power to vote on December 3, 1974 (or on a date subsequent to December 3, 1974, if acquired by a written contract entered into on or before such date) and (2) that does not engage in any activities other than those in which such foreign bank, company, or affiliate may engage by virtue of this subsection or section 4 of the Bank Holding Company Act of 1956; except that the Board by order, after opportunity for hearing, may terminate the authority conferred by this sub-

¹²² *Id.* at 71. It has also been noted that the provisions of the International Banking Act dealing with the Glass-Steagall issue are "not a model of clarity." 77 Hearings, *supra* note 7, at 160 (Statement of George H. Dixon).

section (c) on any such foreign bank or company to engage directly or through an affiliate in any activity otherwise permitted by this subsection (c) if it determines, having due regard to the purposes of this Act and the Bank Holding Company Act of 1956, that such action is necessary to prevent undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices in the United States. Notwithstanding any exercise of the authority conferred upon the Board by this subsection (c), in the case of any such foreign bank or company that engages directly or indirectly through an affiliate in the business of underwriting, distributing, or otherwise buying or selling stocks, bonds, and other securities in the United States, such foreign bank or company may continue to engage in such business in the United States to the extent not prohibited for national banks by paragraph Seventh of section 5136 of the Revised Statutes of the United States (12 U.S.C. 24) and, in addition, may continue to engage in the United States in the business of underwriting and distributing securities to the extent necessary to participate in customary and usual syndicate activities in the United States by the managing underwriters or other underwriters on behalf of all syndicate members in connection with underwritings of such securities so long as the individual selling and distribution activities of any such foreign bank or company (whether direct or indirect through an affiliate) in connection with any such underwriting are confined to jurisdictions other than the United States. Nothing in this subsection (c) shall be construed to authorize any foreign bank or company referred to in this subsection (c), or any affiliate thereof, to engage in activities authorized by this subsection (c) through the acquisition, pursuant to a contract entered into after December 3, 1974, of any interest in or the assets of a going concern engaged in such activities. Any foreign bank or company that is authorized to engage in any activity pursuant to this subsection (c) but, as a result of action of the Board, is required to terminate such activity may retain the ownership of control of shares in any company carrying on such activity for a period of two years from the date on which its authority was so terminated by the Board. As used in this subsection, the term "affiliate" shall mean any company more than 5 per centum of whose voting shares is directly or indirectly owned or controlled or held with power to vote by the specified foreign bank or company.

(d) Nothing in this section shall be construed to define a branch or agency of a foreign bank or a commercial lending company controlled by a foreign bank or foreign company that controls a foreign bank as a "bank" for the purposes of any provisions of the Bank Holding Company Act of 1956, or section 105 of the Bank Holding Company Act Amendments of 1970, except that any such branch, agency or commercial lending company subsidiary shall be deemed a "bank" or "banking subsidiary", as the case may be, for the purposes of applying the prohibitions of section 106 of the Bank Holding Company Act Amendments of 1970 and the exemptions provided in sections 4(c)(1), 4(c)(2), 4(c)(3) and 4(c)(4) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(c) (1), (2), (3), and (4)) to any foreign bank or other company to which subsection (a) applies.