(c) Affect or impair any right or remedies of the United States, or of any person, with respect to any such violation.

§ 1260.185 Amendments.

Amendments to this subpart may be proposed, from time to time, by the Board or by an organization certified pursuant to Section 15 of the Act, or by any interested person affected by the provisions of the Act, including the Secretary.

§ 1260.186 Personal liability.

No member, alternate member, or employee of the Beef Board shall be held personally responsible, either individually or jointly with others, in any way whatsoever to any person for errors in judgment, mistakes, or other acts, either of commission or omission, of such member, alternate, or employee except for acts of dishonesty or willful misconduct.

§ 1260.187 Separability.

If any provision of this subpart is declared invalid or the applicability thereof to any person or circumstances is held invalid, the validity of the remainder of this subpart or the applicability thereof to other persons or circumstances shall not be affected thereby.

Proposed by Community Nutrition Institute

Proposal No. 2

In the appropriate sections, the Beef Research and Information Order shall provide:

(a) That the Secretary shall appoint five consumer advisors to the Beef Board. Such advisors shall be persons determined by the Secretary to be knowledgeable in nutrition and food.

(b) That consumer advisors be reimbursed for necessary and reasonable expenses they incur in performing their duties as advisors to the board.

(c) That consumer advisors be compensated for actual work performed in addition to reimbursement for necessary and reasonable expenses.

Proposed by the Livestock, Poulty, Grain and Seed Division, Agricultural Marketing Service

Proposal No. 3

Make such changes as may be necessary to make the entire order conform with any provisions thereto that may result from this hearing.

Copies of this notice of hearing and the proposed order may be procured from Ralph L. Tapp, Livestock, Poultry, Grain and Seed Division, Agricultural Marketing Service, Room 2084 South Building, United States Department of Agriculture, Washington, D.C. 20250, or from the Hearing Clerk, Room 1077, South Building, United States Department of Agriculture, Washington, D.C. 20250, or may be there inspected.

From the time that a hearing notice is issued until the issuance of a final decision in a proceeding, Department employees involved in the decisional process are prohibited from discussing the merits of the hearing issues on an ex parte basis with any person having an interest in the proceedings. For this particular proceeding the prohibition applies to employees in the following organizational units:

Office of the Secretary of Agriculture.
Office of the Administrator, Agricultural Marketing Service.
Office of the General Counsel.
Livestock, Poultry, Grain and Seed Division, Agricultural Marketing Service (Washington office only).

Procedural matters are not subject to the above prohibition and may be discussed at any time.

Signed at Washington, D.C. on April 17, 1979.

Jerry C. Hill,
Deputy Assistant Secretary.

[Docket No. BRIA-2]
[FR Doc. 79-12465 Filed 4-20-79; 8:45 am]
BILLING CODE 3410-02-M

FEDERAL RESERVE SYSTEM

[12 CFR Part 202]

Equal Credit Opportunity; Application to Credit Scoring

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rulemaking.

SUMMARY: The Board solicits comment on how the specific rules of Regulation B should apply to the following credit scoring system practices: (1) scoring number of jobs or number of sources of income; (2) not scoring the amount of an applicant's income from part-time employment, pension, or alimony; (3) selecting the reasons for adverse action judgmentally; and (4) using reasons for adverse action from the model statement when they do not correspond to the characteristics scored.

DATE: Comments must be received on or before June 20, 1979.

ADDRESS: Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. All comments should refer to docket number R-203.

FOR FURTHER INFORMATION CONTACT: Dolores S. Smith, Section Chief, Division of Consumer Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 (202-452-2412).

SUPPLEMENTARY INFORMATION: The Equal Credit Opportunity Act (ECOA) and its implementing Regulation B differentiate between "demonstrably and statistically sound, empirically derived credit systems" and "judgmental systems" of credit analysis. Credit scoring systems that meet specified tests of statistical validity qualify as demonstrably and statistically sound, empirically derived credit system. All other types of credit analysis constitute judgmental systems.

Regulations B's specific rules represent the Board's judgment about the general effect of selected credit practices on the population at large. When adopting the specific rules, the Board focused principally upon discriminatory practices of judgmental systems. Accordingly, the proper application of the specific rules to credit scoring systems remains unclear.

The Board invites comment on the four issues enumerated in the Summary. Resolving them could entail a variety of regulatory action, including amending Regulation B and issuing official interpretations. Before considering any extensive changes, the Board wishes to encourage a thorough public discussion that will address both the impact of possible changes and the need for any change at all. The options described for each issue are not mutually exclusive and do not constitute the only possible responses. The Board also solicits comment on the general subject of applying Regulation B's specific rules to credit scoring systems. After analysis of the comments received, the Board will determine what issues, if any, warrant its further consideration and what regulatory action appears appropriate.

1. *In developing and using a credit scoring system, what constitutes discounting of income and what consitutes exclusion of consideration of income?*

Section 202.6(b)(5) provides that a "creditor shall not discount or exclude from consideration the income of an applicant . . . because the income is derived from part-time employment. . . ." However, the "creditor may consider the amount and probable continuance of any income. . . ." The Board adopted this rule to prevent discrimination against married women, many of whom work only part-time, and to curtail the practice of arbitrarily

discounting the wife's income on joint applications. For a judgmental system, the rule means that the credit officer must accord reliable amounts of part-time income the same treatment given income from any other source. The Board did not consider how the rule should affect credit scoring systems.

1a. *For example, may a credit scoring system score the fact that an applicant has more than one job or multiple sources of income, and may it score secondary income differently from primary income?*

Assuming that "number of jobs" contributes to a system's predictive power, may the system assign fewer points or less weight to applicants holding multiple jobs (e.g., one—10, two or more—5 points)? Related issues include the proper treatment of the number of income sources and of the amount of income from different types of sources (earned, alimony, pension, dividend, etc.). The Board recognizes that these issues involve competing considerations and that how the question is phrased to some extent dictates the answer.

For example, those who would prohibit assigning negative points for multiple jobs argue that this practice has the effect of disadvantaging several protected classes of applicants. In addition, the literal text of the § 202.6(b)(5) rule could be interpreted to preclude discounting part-time income by type, as well as amount. Finally, to penalize an applicant for fully completing the application (e.g., providing information about part-time employment) may simply seem undesirable when selective omissions (e.g., not providing part-time employment information) would confer a greater probability of obtaining credit.

Conversely, proponents of the practice might show that "number of jobs" predicts creditworthiness. Prohibiting its use reduces system accuracy and therefore increases the aggregate risk of extending credit. Further, the regulation refers to the amount of part-time income, not its mere existence. Finally, the practice of assigning less weight to second jobs may not have the effect of discriminating on a prohibited basis since all manner of applicants "moonlights."

The Board hopes that public comments will bring additional considerations to its attention. At present, it contemplates one or more of the following options for addressing this issue.

A. Interpreting § 202.6(b)(5) as applying only to judgmental systems, thereby authorizing scoring number of jobs.

B. Interpreting the rule to prohibit scoring number of jobs, number of sources of income, or amount of income from different sources.

C. Interpreting the rule as not per se prohibiting the practice, but allowing ECOA enforcement agencies to detemine on a case by case basis whether scoring number of jobs or sources of income has the effect of impermissibly discriminating against an applicant on a prohibited basis.

1b. *How must a scoring system consider the amount of an applicant's income from part-time employment, pension, or alimony?*

Section 202.6(b)(5)'s prohibition on exluding part-time income from consideration also applies to pension and alimony income. These additional provisions seek to protect divorced women and the elderly from discrimination unrelated to their creditworthiness. When adopting them, the Board concentrated on arbitrary behavior by judgmental creditors. It now solicits comment on how this specific rule should apply to credit scoring systems.

Development of a scoring system typically uses statistical techniques to select the characteristics that, taken together, predict the repayment performance of the creditor's recent applicants. A properly designed development process may examine and reject other characteristics as nonpredictive. If secondary income does not contribute to the creditworthiness prediction, must the system score it anyway, or would having included secondary income as a trial characteristic during the intial phases of the development procedure suffice?

Proponents of scoring nonpredictive secondary income interpret § 202.6(b)(5) as requiring explicit treatment of these types of secondary income. They also point out that the section contemplates an individual analysis of the particular applicant's income and precludes assumptions based upon the experience with similar income of prior applicants. Thus, the creditor must consider the fact that a particular applicant can prove the regular receipt of alimony, even if most applicants' alimony does not arrive on schedule.

Opponents object to this interpretation as overliteral. The Board adopted the rule to deter credit officers from using stereotypes in lieu of individual analysis when dealing with divorcees, the elderly, and married women. A scoring system, however, uses only the combination of characteristics that best associate with creditworthiness. If secondary income does not statistically associate with creditworthiness, the government should not make it do so. Requiring a creditor to score a nonpredictive characteristic distorts the validity of the credit analysis process. This increases the creditor's overall risk of doing business and may result in less credit to economically disadvantaged applicants.

The Board invites comment on the issue of how a scoring system should consider the amount of an applicant's income from part-time employment, pension, or alimony, and on possible alternatives for addressing it, including:

A. Exempting credit scoring from the "consideration" rule in § 202.6(b)(5).

B. Deeming inclusion of secondary income as a trial characteristic in the system development process to constitute sufficient consideration.

C. Requiring that any scoring of amount of income include all types of income as a single characteristic.

D. Requiring that scoring systems have a judgmental override that considers secondary income.

E. Requiring positive allocation of points to secondary income regardless of its predictive power.

F. Requiring systems to inclue a subsystem that predicts the reliability of the particular applicant's secondary income.

2. *How must a creditor using a scoring system select the "specific" reasons for adverse action?*

The ECOA and Regulation B provide that, when a creditor takes "adverse action" (e.g., by rejecting a credit request), it must give the applicant either the specific reasons for the action or a disclosure of the right to receive the reasons. Section 202.9(b)(2) of the regulation requires that a statement of reasons suffices if "specific and indicates the principal reasons for the adverse." A statement that the applicant failed to achieve a passing score does not suffice as a specific reason. Receiving the reasons for adverse action gives applicants an opportunity to take remedial action, correct erroneous assumptions of the creditor, and reapply when a mutable attribute changes (e.g., when income increases).

Recent FTC consent decrees contain a requirement that users of scoring systems select their adverse action using a specified mathematical formula. Under these decrees, the creditor must examine the scoring sheet for the rejected application, subtract the applicant's score from the median score for each characteristic, and disclose the four characteristics having the largest differences. The Board's staff, on the other hand, has unofficially interpreted § 202.9(b)(2) to permit judgmental selection of reasons for adverse action, even by creditors using scoring. Thus, the credit officer may select the reasons

from all the information on the application.

Proponents of the former interpretation argue that the scored characteristics alone contribute to the credit decision, and that therefore they comprise the real reasons for adverse action. Permitting the creditor to disclose unscored characteristics from the balance of an application does not provide information the applicant can use to take remedial action. ECOA enforcement agencies also suggest that some creditors use judgmental selection of reasons to conceal discriminatory credit analysis practices. By manually selecting among all the information on the application, they intentionally mislead applicants about the true reasons for their rejection.

Opponents of the mathematical process reason that under a judgmental system the credit officer makes the credit decision and selects the reasons manually. The same officer can also select the reasons where a scoring system makes the initial decision. In addition, some important reasons occur too infrequently for inclusion on the scoring sheet (e.g., bankruptcy), but would be selected by judgmental systems as critical. Finally, a suitable method for selecting reasons for adverse action will vary from case to case, depending upon the nature of the particular credit analysis process. A fixed, mathematical procedure may prove unsuitable in certain cases. For example, a scoring system that allocates half of its possible points for a single characteristic would select this characteristic as the reason so frequently as to obscure its specificity as a reason.

The Board hopes that public comment will more fully explore these considerations. It suggests the availability of a variety of approaches to the problem.

A. Authorizing either mathematical or judgmental selection of reasons for adverse action.

B. Requiring judgmental selection.

C. Requiring that applicants with similar financial characteristics receive similar reasons, but not specifying the method for selecting them.

D. Specifying the exact formula for relating scored characteristics to selection of reasons for adverse action.

3. *Under what circumstances may a creditor employing a credit scoring system use the reasons for adverse action from Regulation B's model statement?*

As noted above, the statute and § 202.9(b)(2) require disclosure of "specific" reasons for adverse action. Section 202.9(b)(2) also provides a model "statement of credit denial, termination, or change," proper use of which satisfies this requirement. The model statement contains twenty categories of reasons for adverse action, including "other, specify." The Board adopted the model statement to facilitate compliance by small creditors.

ECOA enforcement agencies have experienced some difficulties in the specificity with which model reasons must correspond to scored characteristics while still amounting to proper use. The problem arises because scored characteristics have greater specificity than the "pertinent elements of creditworthiness" used in a typical judgmental system. For example, a creditor might score: finance company loans, yes–0, no–15; bank loans, yes–6, no—1; or credit cards from prestigious department stores, none–0, one–4, two or more–16. None of the reasons on the model notice relate closely to any of these specific characteristics. Instead of filling in the "other, specify" line, a creditor may check whichever reason seems to be closest (e.g., insufficient credit references).

Critics of this practice suggest that forcing specific characteristics into model categories of reasons violates the requirement of specificity. The practice of discounting finance company loans relates only indirectly to insufficient credit references. In addition, this mischaracterization or lack of specificity deprives rejected applicants of the opportunity to remedy their credit deficiencies. The critics argue that it therefore constitutes a misuse of the model statement and does not satisfy the specific rule's requirements. Finally, ECOA enforcement agencies suggest that some creditors use the model reasons to mislead applicants about the characteristics scored in order to conceal discriminatory practices. The agencies believe that precise restrictions on proper use of the model statement will reduce this abuse.

Conversely, the legislative history accompanying ECOA indicates that the Congress contemplated only the most general statement of reasons. One of the examples in the legislative history contains only seven reasons. Requiring that disclosed reasons for adverse action correspond exactly to scored characteristics will also disrupt the present operations of creditors that use scoring. Changing procedures and forms will entail extra compliance costs. In addition, increased specificity will mean greater uncertainty as creditors grope to comply with a new standard that lacks precise quantification. How specific is "specific"? Finally, using the model statement to evade the regulation presently constitutes a violation, and the enforcement tools for dealing with such practices already exist.

The Board perceives the question as being one of degree. Consider a system that scores the number of credit references from banks. An applicant with six references from stores, finance companies, and thrift institutions receives no points for them. Checking "insufficient credit references" on the adverse action notice seems insufficiently specific. Diclosing "no bank references" probably would suffice. What intermediate levels of specificity also comply with the requirements of a statement of specific reasons for adverse action, and how can the Board precisely articulate them? The Board envisions one or more of the following alternatives.

A. Increasing the number of reasons on the model statement.

B. Prohibiting creditors that use scoring systems from utilizing the model statement.

C. Deeming "specific" to be the general standard and leaving it to each enforcement authority to determine whether a particular reason conforms to this standard.

D. Promulgating more precise standards for relating scored characteristics to specificity of reasons for adverse action, but leaving the model statement unchanged.

E. Requiring creditors that use scoring systems to disclose that they use scoring, the exact characteristics scored, and the four characteristics for which the applicant lost the most points, in lieu of using the model statement.

Pursuant its authority under § 703 of ECOA, the Board proposes to adopt one or more of the following amendments to Regulation B. The amendments appear sequentially by issue and option. The proposed new language is in italics.

Issue 1a: Section 202.6(b)(5) would be amended to read:

Option A: *In a judgmental system,* a creditor shall not discount or exclude from consideration. . . .

Option B: A creditor shall not discount or exclude from consideration the income of an applicant or the spouse of an applicant because of a prohibited basis or because *of the amount or type of income* derived from part-time employment. . . .

Option C: A creditor shall not discount or exclude from consideration the *amount of* income of an applicant or. . . .

Issue 1b: Section 202.6(b)(5) would be amended to read:

Option A: *In a judgmental system,* a creditor shall not discount or exclude from consideration. . . .

Option B: . . . in evaluating an applicant's creditworthiness. *A demonstrably and statistically sound, empirically derived credit system may consider this income by including it as a trial characteristic during*

the system construction process. Where an applicant relies. . . .

Option C: *In a judgmental system,* a creditor shall not discount or exclude from consideration. . . . *In a demonstrably and statistically sound, empirically derived credit system that considers the amount of income of an applicant or the spouse of an applicant, the creditor shall consider all reliable income as a single characteristic.* Where an applicant relies. . . .

Option D: . . . in evaluating an applicant's creditworthiness. *A demonstrably and statistically sound, empirically derived credit system shall comply with this requirement by using a judgmental override that considers such income.* Where an applicant relies. . . .

Option E: . . . in evaluating an applicant's creditworthiness. *A demonstrably and statistically sound, empirically derived credit system shall comply with this requirement by allocating at least x per cent of the possible total points to receipt of such income.*

Issue 2: Section 202.9(b)(2) would be amended to add a new sentence at its end:

Option A: *A creditor may select the reasons either judgmentally or by using a mathematical formula.*

Option B: *A creditor using a demonstrably and statistically sound, empirically derived credit system shall select the reason(s) judgmentally.*

Option C: *A creditor using a demonstrably and statistically sound, empirically derived credit system shall select the reason(s) using a procedure that will result in applicants with similar financial characteristics receiving identical reasons.*

Option D: *A creditor using a demonstrably and statistically sound, empirically derived credit system shall select as reasons up to four characteristics on which the applicant's score differed most from the maximum possible score.*

Issue 3: Section 202.9(b)(2) would be amended as follows:

Option B: . . . for the adverse action. *A judgmental creditor may use all or a portion of the sample form printed below.* . . .

Option D: . . . for the adverse action. *A statement's reasons are specific if a reasonable consumer receives sufficient information to determine the changes in characteristics that would have resulted in approval of the application.* A creditor may formulate. . . .

Option E: . . . for the adverse action. A *judgmental* creditor may formulate its own statement of reasons. . . . *A creditor using a demonstrably and statistically sound, empirically derived credit system must disclose the use of the system, the manner of its operation, the applicant's score, the passing score, the maximum possible score, and the characteristics scored.*

* * * * *

By order of the Board of Governors, April 13, 1979.

Theodore E. Allison,

Secretary of the Board.

[Reg. B; Docket No. R-203]

[FR Doc. 79-12515 Filed 4-20-79; 8:45 am]

BILLING CODE 6210-01-M

[12 CFR Part 204]

Reserve Requirements on Federal Funds and Repurchase Agreement Time Deposits of Member Banks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board proposes to restructure its reserve requirements as applied to certain borrowings by member banks. Under the proposed restructuring, member banks would be required to maintain a 3 percent reserve against borrowings from domestic offices of nonmember banks and other depository institutions whose liabilities are not subject to reserve requirements and from the United States Government (and its agencies), as well as a 3 percent reserve against certain repurchase agreements on U.S. government and agency securities. Currently, such liabilities are exempt from the Board's reserve requirements.

DATE: Comments must be received by May 18, 1979.

ADDRESS: Comments should be addressed to Theodore E. Allison, Secretary of the Board, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. Comments should contain Docket No. R-0218.

FOR FURTHER INFORMATION CONTACT: Allen L. Raiken, Associate General Counsel, Legal Division (202/452-3625), or Gilbert T. Schwartz, Assistant General Counsel, Legal Division (202/452-3623, Board of Governors of the Federal Reserve System.

SUPPLEMENTARY INFORMATION: The Board of Governors proposes to amend its Regulation D, Reserves of Member Banks (12 CFR 204) to restructure reserve requirements as applied to certain borrowings and repurchase agreements entered into by member banks.

Currently, borrowings by member banks from domestic offices of other banks are not defined as deposits and are not subject to reserve requirements. Also, borrowings by member banks from the United States government (principally in the form of Treasury tax and loan account note balances) and its agencies have not been regarded as deposits subject to reserve requirements. Under the Board's proposal, member bank borrowings from the domestic offices of other banks whose liabilities are not subject to reserve requirements and from the U.S. government and its agencies would be treated as a new category of time deposit subject to a 3 percent reserve requirement.

The term "bank" has been regarded as including commercial banks, savings banks, savings and loan associations, cooperative banks, the Export-Import Bank, and Minbanc Capital Corporation. (See 12 CFR 217.137). For purposes of reserve requirements (and interest rate restrictions) it is also proposed that the term "bank" be expanded to include credit unions. Member bank borrowings from domestic offices of other member banks or other organizations that are or may be required by the Board to maintain reserves and from Federal Reserve Banks would continue to be exempt from reserve requirements. The institutions that currently are subject to reserve requirments include Edge Corporations (12 U.S.C. 615), Agreement Corporations (12 U.S.C. 601-604a), and operations subsidiaries of member banks (12 CFR 204.117). In addition, pursuant to § 7 of the International Banking Act of 1978 (Pub. L. 95-369), the Board may subject U.S. branches and agencies of foreign banks to reserve requirements. The exemption is believed appropriate to facilitate the reserve adjustment process of member banks and to avoid the possibility of imposing double reserve requirements on liabilities that already may be subject to reserve requirements.

The Board's proposal would also affect member bank borrowings in the form of repurchase agreements based on U.S. government and agency securities. Currently, such repurchase agreements entered into by a member bank with any entity are not deposits and are not subject to reserve requirements. Under the Board's proposal, such obligations would be regarded as deposits and would be subject to a 3 percent reserve requirement. However, repurchase agreements entered into by a member bank with domestic banking offices of other member banks or organizations subject to reserve requirements and with the Federal Reserve System would continue to be exempt from reserve requirements.

In order to continue to facilitate the activities of member bank dealers in the U.S. government and agency securities markets, and to provide competitive equality between bank and nonbank dealers, the Board's proposal would regard repurchase agreements entered into with institutions not subject to reserve requirements as time deposits only when the amount of such repurchase agreements exceeds the amount of U.S. government and agency securities held by the member bank in

its own trading account. A member bank's trading account represents the U.S. and agency securities that it holds for its dealer transactions—i.e., securities are purchased with the intention that they will be resold rather than held as an investment. Public comment is requested on appropriate limitations on, or other descriptions of, member bank trading accounts.

It is also proposed that the 3 per cent reserve requirement apply to any obligation that arises from a borrowing by a member bank for one busines day from a dealer in securities whose liabilities are not subject to the reserve requirements of the Federal Reserve Act of proceeds of a transfer of deposit credit in a Federal Reserve Bank (or other immediately available funds), received by such dealer on the date of the loan in connection with clearance of securities transactions.

The proposed actions are designed to establish more effective control over growth of bank credit. Approximately 20 per cent of the growth in commercial bank credit during the past six months has been financed by exempt borrowings in the form of Federal funds and repurchase agreements on U.S. government and agency securities. It is anticipated that the proposed reserve requirements would moderate the growth of commercial bank credit financed through the issuance of these types of bank liabilities.

All comments and information on this proposal should be submitted in writing to Theodore E. Allison, Secretary of the Board of Governors of the Federal Reserve System, Washington, D.C. 20551, to be received by May 18, 1979. All material submitted should include the Docket Number R-0218. Such material will be made available for inspection and copying upon request except as provided in section 261.6(a) of the Boards's Rules Regarding Availability of Information (12 CFR 261.6(a)).

Pursuant to its authority under Section 19 of the Federal Reserve Act (12 U.S.C. 461) to define the term deposit and to prescribe reserve ratios for member banks, the Board amends Regulation D (12 CFR 204) as follows:

1. Section 204.1 is amended by revising subparagraphs (b) and (f) as set forth below and by deleting subparagraph (4) and renumbering subparagraph (5) as subparagraph (4).

§ 204.1 Definitions.

* * * * *

(b) *Time deposits.* The term "time deposits" means "time certificates of deposit," "time deposits, open account," and "savings deposit," as defined below; except that for the purposes of § 204.5(b) "time deposits" shall have the meaning set forth therein.

* * * * *

(f) *Depositis as including certain promissory notes and other obligations.* For the purposes of this Part, the term "deposits" also includes a member bank's liability on any promissory not, acknowledgement of advance, due bill, banker's acceptance, repurchase agreements, or similar obligation (written or oral) that is issued or undertaken by a member bank as a means of obtaining funds to be used in its banking business except any such obligation that:

(1) is issued to (or undertaken with respect to) and held for the account of (i) a domestic banking office[6] or agency of another member bank or other organization whose liabilities are or may be subject to the reserve requiremnts of the Federal Reserve Act[6a] or (ii) a Federal Reserve Bank;

(2) is a repurchase agreement arising from a transfer of direct obligations, of, or obligations that are fully guaranteed as to principal and interest by the United States or any agency thereof (except any obligation that is issued to a domestic banking office or agency of another member bank or other organization whose liabilities are or may be subject to the reserve requirements of the Federal Reserve Act[6a] or to a Federal Reserve Bank) to the extent that the amount of such repurchase agreements does not exceed the total amount of United States and agency securities held by the member bank in its trading account;

* * * * *

2. Section 204.5 is amended to read as follows:

§ 204.5 Reserve requirements.

(a) *Reserve percentage.* Pursuant to the provisions of section 19 of the Federal Reserve Act and § 204.2(a) and subject to paragraphs (b) through (e) of this section, * * *

* * * * *

(b) *Reserve percentages against Federal funds and repurchase time deposits.* Deposits represented by the following shall be "time deposits," upon which a member bank shall maintain reserve balances of 3 per cent in accordance with § 204.2 and 204.3:

(1) Any deposit described in § 204.1(f) with a maturity of one day or more (including deposits subject to withdrawal after one or more day's notice) in the form of a promissory note, acknowledgement of advance, due bill, bankers' acceptance, repurchase agreement, or similar obligation (written or oral) issued to and held for the account of a domestic banking office or agency of another commercial bank or trust company, savings bank mutual or stock), a building or savings and loan association, a cooperative bank, a credit union, or the United States or an agency thereof, the Export-Import Bank of the United States, and Minbanc Capital Corporation;

(2) Any deposit described in § 204.1(f) that is a repurchase agreement arising from a transfer of direct obligations of, or obligaions that are fully guranteed as to principal and interest, by the United States or any agency thereof that the member bank is obligated to repurchase;

(3) Any obligation that arises from a borrowing by a member bank from a dealer in securities that is not a member bank or other organization whose liabilities are or may be subject to the reserve requirements of the Federal Reserve Act, for one business day, of proceeds of a transfer of deposit credit in a Federal Reserve Bank (or other immediately available funds), received by such dealer on the date of the loan in connection with clearance of securities transactions.

* * * * *

(f) *Currency and coin.* The amount of a member bank's currency and coin shall be counted as reserves in determining compliance with the reserve requirements of this section.

By order of the Board of Governors of the Federal Reserve System, April 13, 1979.

Theodore E. Allison,
Secretary of the Board.

[Regulation D; Docket No. R-0128]
[FR Doc. 79-12517 Filed 4-20-79; 8:45 am]
BILLING CODE 6210-01-M

[6] * * *

[6a] Liabilities of Edge Corporations, Agreement Corporations, and operations subsidiaries of member banks are subject to reserve requirements of the Federal Reserve Act. As specified by the International Banking Act of 1978, liabilities of U.S branches or agencies of foreign banks may be subject to reserve requirements of the Federal Reserve Act.

FEDERAL DEPOSIT INSURANCE CORPORATION

[12 CFR Parts 330, 346]

Foreign Banks

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Proposed rule.

SUMMARY: The FDIC proposes to promulgate a new regulation (Part 346)

and amend an existing regulation (Part 330) to implement the International Banking Act of 1978 (the "Act", 12 U.S.C. 3101 *et seq.*). The Act requires, in part, that certain branches of foreign banks be insured by the FDIC. The proposed regulations establish rules for determining whether a State branch must be insured and set out the FDIC's requirements for insured branches.

DATES: Comments must be received by the FDIC by May 25, 1979.

ADDRESS: Comments should be addressed to Mr. Hoyle L. Robinson, Acting Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, D.C. 20429.

FOR FURTHER INFORMATION, CONTRACT: Margaret M. Olsen, Attorney, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, D.C. 20429 (202–389–4433).

SUPPLEMENTARY INFORMATION: On December 27, 1978, the FDIC published for comment preliminary staff conclusions as to several issues regarding implementation of the Act (the "Advance Notice", 43 F.R. 60279). The FDIC received some 28 written comments on the Advance Notice. The majority of the comments were from the foreign banking community.

Under § 6 of the Act, certain branches of foreign banks are required to obtain Federal deposit insurance. In particular, deposit insurance is required for a Federal branch that accepts deposits of less than $100,000 and for a State branch that accepts deposits of less than $100,000 if it is located in a State which requires deposit insurance for State-chartered banks. Exemptions from the insurance reqirement may be granted either by regulation or by order of the Comptroller of the Currency, in the case of a Federal branch, or the FDIC, in the case of a State branch, if the branch is not engaged in a domestic retail deposit activity requiring insurance protection.

Section 6 also makes numerous amendments to the Federal Deposit Insurance Act (the "FDI Act"). Some of these amendments apply only to foreign banks having insured branches; other amendments apply existing requirements for domestic banks to foreign banks having insured branches. The amendments to the FDI Act dealt with in the proposed regulation are: (1) A requirement that the foreign bank give a commitment for examination; (2) A requirement that the foreign bank pledge assets to the FDIC or provide a surety bond; (3) rules for the insurance of deposits in the branch; and, (4) rules for the assessment of deposits by the FDIC.

Brief Analysis of Part 346

Subpart B of proposed Part 346 establishes rules for determining which State branches must obtain deposit insurance. Basically, branches engaged in a "retail" deposit activity must be insured while branches engaged in a "wholesale" deposit activity do not have to be insured. These rules apply to State branches; the Comptroller of the Currency will establish rules for determing which Federal branches are required to be insured. Federal branches deemed by the Comptroller to require insurance must, however, apply to the FDIC for insurance. Subpart B also includes a requirement that where one branch of a foreign bank becomes insured, every branch of that bank must become insured (except for branches operating under an agreement with the Federal Reserve to accept only those deposits permitted an Edge corporation). This condition for insurance applies to both Federal and State branches.

Subpart C establishes rules that apply to foreign banks which operate insured State or Federal branches. These rules requires a foreign bank having an insured branch to: (1) Provide FDIC with information regarding the bank's activities outside of the United States and allow FDIC to examine the bank's activities in the United States; (2) maintain records in an appropriate manner; (3) pledge assets under terms acceptable to the FDIC; and (4) maintain assets at the branch equal in value to the branch's liabilities. Rules for assessing the deposits of an insured branch are also set out.

Discussion of Issues

1. *Operation of insured and uninsured branches.* FDIC's Board of Directors proposes to grant insurance to one branch of a foreign bank only on the condition that every branch of the bank in the United States be insured. This condition would not apply to a branch located outside of the foreign bank's home State and operating under an agreement with the Federal Reserve to accept only those deposits permitted an Edge corporation. The Board is concerned that public confusion might result were a foreign bank to have insured branches and uninsured branches, particularly in the same State. Under such circumstances, a depositor might not realize that a deposit in one branch is insured but that a deposit in another branch of the same bank would not be insured. This condition is believed necessary to protect the unsophisticated depositor. This issue was not addressed in the Advance Notice and the Board specifically requests comments on this issue.

2. *Mandatory Insurance.* Under § 6 of the Act, a State branch must be insured if the branch accepts deposits of less than $100,000 and if the branch is located in a State that requires State banks to be insured. The Board proposes that the initial deposit be determinative of this dollar limitation. The initial desposit is defined as the first deposit transaction between the branch and the depositor. Accounts which are held by the depositor in the same right and capacity may be added together for the purpose of determining the amount of the initial deposit. Branches established before September 17, 1978 would not be subject to the initial deposit rule until September 16, 1979 and such a branch could retain deposits accepted before the September 1979 date without having to become an insured branch. Most comments on the Advance Notice agreed that the initial deposit is appropriate for determining the statutory dollar limitation.

In considering whether a State requires deposit insurance for State banks, FDIC's Board of Directors proposes to look to requirements imposed by statute, regulation or policy. The Board considers a requirement by policy to be as binding on State banks as a statute or regulation, otherwise foreign banks would have a competitive advantage over State banks. The comments on this issue were divided as to whether policy should be included as a State requirement.

3. *Exemptions from the insurance requirement.* The Board proposes two procedures for exempting from the insurance requirement branches which accept initial deposits of less than $100,000. First, the branch can limit its deposit activities to those described in proposed § 346.7(a). Under this section, an uninsured branch may accept deposits from any commercial concern (except a small domestic business), any governmental unit, any international organization or any deposit which may be accepted by an Edge corporation. An uninsured branch may also issue drafts or checks of less than $100,000 (except money orders or traveler's checks issued to natural persons). In addition, an uninsured branch may accept deposits of less than $100,000 from any person so long as such deposits do not exceed 2% of the branch's total deposits. This permits the branch to accept deposits from corporate officers, embassy or consular personnel and branch employees without having to be insured.

Based on comments received, the list of exempt deposit activities was

expanded from those listed in the Advance Notice. Most commenters requested that an uninsured branch be permitted to accept accounts from corporate officers, embassy or consular personnel, and branch employees, arguing that such deposits are incident to a wholesale activity.

In addition, in response to several comments, a procedure has been established to allow a foreign bank to request an exemption from the insurance requirement for a specific branch. This procedure will allow the bank to operate an uninsured branch when the Board determines that the deposit activities at that branch do not require insurance protection. Branches which are exempt under either procedure must notify their depositors that their deposits are not insured by the FDIC.

Also, as provided in § 5 of the Act, a branch located outside of the foreign bank's home state is not required to be insured whenever the bank has entered into an agreement with the Federal Reserve to accept at that branch only those deposits that are permissible for an Edge corporation.

4. *Agreement to provide information and for examination.* Under § 10(b) of the FDI Act a foreign bank, as a condition of insurance of a branch, must give the FDIC a written commitment that the FDIC may examine the bank and its affiliates to the extent the FDIC deems necessary. The FDIC is aware that most foreign banks would be prohibited, or at least restricted, by law or policy of the country of the bank's domicile from providing such a commitment. Were the FDIC to require a commitment allowing the FDIC to conduct a full examination of the bank, it is probable no foreign bank could operate an insured branch. This result clearly was not intended by Congress. Thus, the FDIC proposes that a foreign bank agree to provide the FDIC with information regarding the affairs of the bank and its affiliates which are located outside of the United States. As to activities within the United States, the bank shall agree to allow the FDIC to examine the affairs of the bank and its affiliates. This issue was not addressed in the Advance Notice and specific comment is requested on it.

5. *Pledge of asset requirements.* Under § 5(c) fo the FDI Act the FDIC may require a foreign bank to pledge assets or deliver a surety bond to the FDIC in order to protect the deposit insurance fund against risk of loss from insuring deposits in a branch. Under the proposed regulation, the FDIC will require a pledge of assets equal in value to 10% of the insured branch's total liabilities (with minor adjustments). If the State or Federal licensing authority of the branch requires the branch to pledge assets, the branch may deduct from the amount required to be pledged to the FDIC the amount pledged to the licensing authority so long as the FDIC retains a pledge of assets equal in value at least to 5% of the branch's liabilities. Whenever the FDIC is obligated to pay the insured deposits of an insured branch, the pledged assets will become FDIC's property to be used to the extent necessary to protect the insurance fund.

It is proposed that the pledged assets be held at a depository acceptable to the FDIC and under an agreement consistent with the terms set out in the regulation. The proposed regulation also sets out the kinds of assets acceptable to the FDIC.

Comments on the Advance Notice on this issue were generally concerned about the FDIC taking a pledge of assets separate from that of the States or the Comptroller of the Currency. The Board, however, is concerned that a joint pledge would not provide additional protection to the deposit insurance fund. This additional protection may be necessary since most of the bank's activities, assets, and personnel are largely outside of the United States.

6. *Asset Maintenance.* The Board is proposing to establish an asset maintenance rule for insured branches. The Board is concerned that without such a rule, in the event of liquidation of the branch, sufficient assets would not be available to protect creditors of the branch. As proposed, an insured branch would be required to maintain, on an average daily basis, assets equal in book value to the amount of the branch's liabilities. For the purpose of this rule, the branch must exclude as an asset (1) amounts due from related entities; (2) assets classified by the examining authorities as "loss" and half the value of those classified as "doubtful"; and, (3) correspondent accounts when there is no valid waiver of offset agreement. In addition, if the branch does not have actual possession of an asset, the branch may include it only if the branch holds title and if proper records are maintained. In determining its liabilities, the branch must exclude amounts due to related entities.

Most comments on this issue in the Advance Notice argued that the FDIC should not impose an asset maintenance rule.

7. *Assessment Base.* The Board proposes to assess all deposits in an insured branch except for deposits of related entities. Assessments would be in accordance with Part 327 of FDIC's rules.

8. *Insured Deposit.* Although the Act permits the FDIC's Board of Directors to limit insurance to certain categories of depositors, the Board is concerned that, if insurance coverage were so limited, it would be virtually impossible to administer in the event of the liquidation of the branch. Instead, it is proposed that deposits (except for those of related entities) be insured to the statutory limit ($40,000 per depositor).

Most comments on the Advance Notice were against the expansion of insurance coverage. Several commenters were in favor of all deposits being insured. Those that opposed the expansion believed that Congress intended to limit the coverage.

Accordingly, the Board proposes to add new Part 346 (12 CFR Part 346) and amend Part 330 of FDIC's rules and regulations as set out below.

By Order of the Board of Directors, April 16th, 1979.

Federal Deposit Insurance Corporation.

Hoyle L. Robinson

Acting Executive Secretary.

PART 330—CLARIFICATION AND DEFINITION OF DEPOSIT INSURANCE COVERAGE

Part 330 is amended by adding a new § 330.0; by revising the third sentence of § 330.1(a); and, by adding a new paragraph (d) to § 330.1 to read as follows:

§ 330.0 Definition.

For the purpose of this Part 330 the term "insured bank" includes an insured branch of a foreign bank.

§ 330.1 General principles applicable to determining insurance of deposit accounts.

(a) *General.* * * * Insofar as rules of local law enter into such determinations, the law of the jurisdiction in which the insured bank's principal office is located shall govern, except where the insured bank is an insured branch of a foreign bank, in which case the law of the jurisdiction where the insured branch is located shall govern.

* * * * *

(d) *Insured branches of foreign banks.* (1) Except as provided in § 330.1(d)(3) deposits in an insured branch of a foreign bank which are payable in the United States shall be insured in accordance with the rules of this part.

(2) Depositis held by an insured depositor in any insured branch or insured branches of the same foreign bank shall be added together for deposit insurance purposes.

(3) Deposits of the foreign bank or any office, branch or agency of and wholly owned (except for a nominal number of directors' shares) subsidiary shall not be insured.

PART 346—FOREIGN BANKS

Subpart A—Definitions

Sec.
346.1 Definitions.

Subpart B—Insurance of Depostis

346.2 Scope.
346.3 Restrictions on operation of insured and uninsured branches.
346.4 General principles applicable to determining which State branches must be insured.
346.5 Insurance requirement.
346.6 Interstate branches.
346.7 Exemptions from the insurance requirement.
346.8 Notification to depositors.
346.9 Optional insurance
346.10–346.15 [Reserved]

Subpart C—Foreign Banks Having Insured Branches

346.16 Scope.
346.17 Agreement as to information provided by an examination of the bank.
346.18 Records.
346.19 Pledge of assets.
346.20 Asset maintenance.
346.21 Deductions from the assessment base.

Authority: Secs. 5, 6, 13, Pub. L. 95–369, 92 Stat. 613, 614, 624 (12 U.S.C. 3103, 3104, 3108); secs. 5, 7, 9, 10, Pub. L. 797, 64 Stat. 876, 877 881, 882 (12 U.S.C. 1815, 1817, 1819, 1820).

Subpart A—Definitions

§ 346.1 Definitions.

For the purposes of this part:

(a) "Foreign bank" means any company organized under the laws of a foreign country, a territory of the United States, Puerto Rico, Guam, American Samoa or the Virgin Islands, which engages in the business of banking, or any subsidiary or affiliate, organized under such laws, of any such company. the term includes foreign commercial banks, foreign merchant banks and other foreign institutions that engage in banking activities usual in connection with the business of banking in the countries where such foreign institutions are organized and operating.

(b) "Foreign country" means any country other than the United States and includes any colony, dependency or possession of any such country.

(c) "State" means any State of the United States or the District of Columbia.

(d) "Branch" means any office or place or busines of a foreign bank located in any State of the United States at which deposits are received.

(e) "Federal branch" means a branch of a foreign bank established and operating under the provisions of § 4 of the International Banking Act of 1978 (12 U.S.C. 3102).

(f) "State branch" means a branch of a foreign bank established and operating under the laws of any State.

(g) "Insured branch" means a branch of a foreign bank any deposits of which branch are insured in accordance with the provisions on the Federal Deposit Insurance Act.

(h) "Uninsured branch" means a branch of a foreign bank deposits of which branch are not insured in accordance with the provisions of the Federal Deposit Insurance Act.

(i) "Insured bank" means any bank, including a foreign bank having an insured branch, deposits of which are insured in accordance with the provisions of the Federal Deposit Insurance Act.

(j) "Home State" of a foreign bank means the State so determined by the election of the foreign bank, or in default of such election, by the Board of Governors of the Federal Reserve System.

(k) "Initial deposit" means the first deposit transaction between a depositor and the branch. The initial deposit may be placed into different kinds of deposit accounts, such as demand, savings or time. Deposit accounts that are held by a depositor in the same right and capacity may be added together for the purposes of determining the dollar amount of the initial depost.

(l) "Domestic retail deposit activity" means the acceptance by a State branch of any initial depost of less than $100,000.

(m) A "majority owned subsidiary" means a company the voting stock of which is 50 percent or more owned or controlled by another company.

(n) "Affiliate" means the same as in Section 2 of the Banking Act of 1933 (12 U.S.C. 221a).

(o) "Depository" means any insured State bank or national bank.

Subpart B—Insurance of Deposits

§ 346.2 Scope.

(a) This subpart B implements the insurance provisions of § 6 of the International Banking Act of 1978 (12 U.S.C. 3104). It sets out the FDIC's rules regarding deposit activities requiring a State branch to be an insured branch; deposit activities not requiring a State branch to be an insured branch; procedures for a State branch to apply for an exemption from the insurance requirement; and, depositor notification requirements.[1] It sets out the FDIC's policy regarding the operation of insured and uninsured branches, whether State or Federal, by a foreign bank and it provides that any branch has the option of applying for insurance.

(b) Any application for insurance under this subpart should be filed in accordance with Part 303 of the FDIC's Rules and Regulations.

§ 346.3 Restriction on operation of insured and uninsured branches.

The Board of Directors will not insure deposits in any branch of a foreign bank unless the foreign bank agrees that every branch established or operated by the foreign bank in the United States will be an insured branch: *Provided,* That this restriction does not apply to a branch subject to an agreement with the Board of Governors of the Federal Reserve System under § 5 of the International Banking Act (12 U.S.C. 3103).

§ 346.4 General principles applicable to determining which State branches must be insured.

(a) Each State branch of a foreign bank shall be considered separate for the purposes of this Subpart B.

(b) Any remote service facility operated by a foreign bank will not be deemed a separate State branch for the purposes of this Subpart B. Any remote service facility established for the benefit of a State branch that is required to be an insured branch will be deemed part of that State branch.

§ 346.5 Insurance requirement.

(a) *General rule.* Except as provided in § 346.6 or § 346.7, a foreign bank shall not establish or operate any State branch which is not an insured branch whenever—

(1) The branch is engaged in a domestic retail deposit activity; and,

(2) The branch is located in a State which requires a bank organized and existing under State law to have deposit insurance whenever the bank accepts deposits from the general public. A State requirement is one imposed by statute or by State banking department regulation or policy.

(b) *Branches established before September 17, 1978.* A foreign bank which established a State branch before September 17, 1978 may operate that branch as an uninsured branch until

[1] These rules do not apply to a Federal branch; the Comptroller of the Currency's regulations establish such rules for Federal branches. Federal branches deemed by the Comptroller to require insurance must apply to the FDIC for insurance.

September 16, 1979 without restriction on its deposit activities. After September 16, 1979 the provisions of paragraph (a) of this section shall be applicable to that branch.

§ 346.6 Interstate branches.

A foreign bank may operate any State branch as an uninsured branch whenever—

(a) The branch is located outside of the home State of the foreign bank; and,

(b) The foreign bank has entered into an agreement with the Board of Governors of the Federal Reserve System to accept at that branch only those deposits as would be permissible for a corporation organized under Section 25(a) of the Federal Reserve Act (12 U.S.C. 611 *et seq.*) and implementing rules and regulations administered by the Board of Governors (12 CFR Part 211).

§ 346.7 Exemptions from the insurance requirement.

(a) *Deposit activities not requiring insurance.* A State branch will not be deemed to be engaged in a domestic retail deposit activity which requires the branch to be an insured branch under § 346.5 if the acceptance of initial deposits in an amount of less than $100,000 is limited to the following:

(1) Any sole proprietorship or any business entity, including any corporation, partnership, association or financial institution, which engages in commercial activity for profit: *Provided,* That this category does not include a business which is organized under the laws of any State or the United States, majority owned by United States citizens or residents and that has total assets not exceeding $1,500,000 at the most recent fiscal year statement as of the date of initial deposit. The $1,500,000 asset test is applicable to the depositor's combined financial interests including the business activities of an individual or parent company and its majority owned subsidiary(s) and affiliate(s).

(2) Any governmental unit, including the United States government, any State government, any foreign government and any political subdivision or agency of the foregoing.

(3) Any non-profit organization which is organized under the laws of a foreign country.

(4) Any international organization membership in which is comprised of two or more nations.

(5) Any other depositor but only if (i) the aggregate amount of deposits under this subparagraph (5) does not exceed 2 percent of the branch's total deposits, excluding deposits of other offices, branches, agencies or wholly owned subsidiaries of the bank, and (ii) the branch does not solicit deposits from the general public.

(6) Any deposit that the Board of Governors of the Federal Reserve System permits a corporation organized under Section 25(a) of the Federal Reserve Act (12 U.S.C. 611 *et seq.*) to accept under the rules and regulations promulgated by the Board of Governors (12 CFR Part 211).

(7) Any draft or check issued by the branch; *Provided,* That this category does not include any money order or traveler's check issued to a natural person.

(b) *Application for an exemption.* (1) Whenever a foreign bank proposes to accept at a State branch initial deposits of less than $100,000 and such deposits are not otherwise excepted under paragraph (a) of this section, the foreign bank may apply to the FDIC for consent to operate the branch as an uninsured branch. The Board of Directors may exempt the branch from the insurance requirement if the branch is not engaged in domestic retail deposit activities requiring insurance protection. The Board of Directors will consider the size and nature of depositors and deposit accounts in making this determination.

(2) Any request for an exemption under paragraph (b) of this section should be in writing and authorized by the board of directors of the foreign bank. The request should be filed with the Regional Director of the FDIC Regional Office where the branch is located.

(3) The request should detail the kinds of deposit activities the branch proposes to engage in, the expected source of deposits and the manner in which deposits will be solicited.

§ 346.8 Notification to depositors.

Any State branch that is exempt from the insurance requirement pursuant to § 346.7 shall—

(a) Display conspicuously at each window or place where deposits are usually accepted a sign stating that deposits are not insured by the FDIC; and

(b) Include in bold face, conspicuous type on each signature card, passbook and instrument evidencing a deposit the statement "This deposit is *NOT* insured by the FDIC."

§ 346.9 Optional insurance.

A foreign bank may apply to the FDIC for deposit insurance for any State branch that is not otherwise required to be insured under § 346.5 or for any Federal branch that is not otherwise required to be insured under the rules and regulations of the Comptroller of the Currency.

§§ 346.10–346.15 [Reserved].

Subpart C—Foreign Banks Having Insured Branches

§ 346.16 Scope.

This Subpart C sets out the rules that apply only to a foreign bank that operates or proposes to establish an insured State or Federal branch. These rules relate to: an agreement to provide information and for an examination; record-keeping; pledge of assets; asset maintenance; and deductions from the assessment base.

§ 346.17 Agreement as to information provided by and examination of the bank.

(a) A foreign bank that applies for insurance for any branch shall agree in writing to the following terms: (1) The foreign bank will provide the FDIC with information regarding the affairs of the bank and its affiliates which are located outside of the United States as the FDIC from time to time may request to (i) determine the relations between the insured branch and the bank and its affiliates and (ii) assess the financial condition of the bank as it relates to the insured branch. If the laws of the country of the bank's domicile or the policy of the Central Bank or other banking authority prohibit or restrict the foreign bank from entering into this agreement, the foreign bank shall agree to provide information to the extent permitted by such law or policy. Information provided shall be in the form requested by the FDIC and shall be made available in the United States. The Board of Directors will consider the existence and extent of this prohibition or restriction in determining whether to grant insurance and may deny the application if the information available is so limited in extent that an unacceptable risk to the insurance fund is presented.

(2) The FDIC may examine the affairs of any office, agency, branch or affiliate of the foreign bank located in the United States as the FDIC deems necessary to (i) determine the relations between the insured branch and such offices, agencies, branches or affiliates and (ii) assess the financial condition of the bank as it relates to the insured branch. The foreign bank shall also agree to provide the FDIC with information regarding the affairs of such offices, agencies, branches or affiliates as the FDIC deems necessary. The Board of Directors will not grant insurance to any branch if the foreign bank fails to enter

into an agreement as required under this subparagraph (2).

(b) The agreement shall be signed by an officer of the bank who has been so authorized by the foreign bank's board of directors. The agreement and the authorization shall be included with the foreign bank's application for insurance. Any agreement not in English shall be accompanied by an English translation.

(c) The provisions of this section do not apply to a bank organized under the laws of Puerto Rico, Guam, American Samoa or the Virgin Islands which is an insured bank other than by reason of having an insured branch.

§ 346.18 Records.

(a) *In English.* The records of each insured branch shall be kept in the words and figures of the English language.

(b) *Separate records.* The records of each insured branch shall be kept as though it were a separate entity, with its assets and liabilities separate from the other operations of the head office, other branches or agencies of the foreign bank and its subsidiaries or affiliates.

(c) *Exemption.* The provisions of this section do not apply to a bank organized under the laws of Puerto Rico, Guam, American Samoa or the Virgin Islands which is an insured bank other than by reason of having an insured branch.

§ 346.19 Pledge of assets.

(a) *Purpose.* A foreign bank that has an insured branch shall be required to pledge assets for the benefit of the FDIC or its designee(s). Whenever the FDIC is obligated to pay the insured deposits of an insured branch, the assets pledged under this section shall become the property of the FDIC to be used to the extent necessary to protect the deposit insurance fund.

(b) *Amount of assets to be pledged.* (1) A foreign bank shall pledge assets equal to ten percent of the insured branch's total liabilities as set out in the insured branch's most recent quarterly report of condition. In determing the total liabilities, the branch may exclude amounts due and other liabilities to other offices, agencies or branches and wholly owned (except for a nominal number of directors' shares) subsidiaries of the foreign bank only if claims of other offices, agencies, branches and wholly owned (except for a nominal number of directors' shares) subsidiaries of the foreign bank are subordinated by law or agreement to the claims of other creditors of the branch. Whenever a state licensing authority or the Comptroller of the Currency require the bank to pledge assets, the foreign bank may deduct from the amount of assets required to be pledged to the FDIC the amount of assets pledged to the State or the Comptroller of the Currency but such deduction may not be greater than assets equal to five percent of the branch's total liabilities. Adjustments to the amount pledged shall be made within two business days after the date required for filing the report of condition.

(2) The initial ten percent deposit for a newly established insured branch shall be based on the branch's projection of liabilities at the end of the first year of its operation.

(3) The FDIC may require a foreign bank to pledge additional assets whenever the FDIC determines the foreign bank's or any branch's condition is such that the assets pledged under § 346.19(b) (1, 2) or any surety bond provided under § 346.19(g) will not adequately protect the deposit insurance fund.

(c) *Depository.* A foreign bank in carrying out the requirements of this section shall deposit pledged assets for safekeeping at any depository which is located in the same the State as the insured branch and which is acceptable to the FDIC.

(d) *Assets that may be pledged.* Subject to the right of the FDIC to require substitution, a foreign bank may pledge any of the following kinds of assets.

(1) Certificates of deposit that are payable in the United States and that are issued by federally or State chartered institutions which have executed a valid waiver of offset agreement: *Provided,* That the maturity of any given certificate is not greater than one year;

(2) Interest bearing bonds, notes, debentures or other obligations of the United States or any agency or instrumentality thereof;

(3) Interest bearing bonds, notes or debentures guaranteed by the United States government or any agency or instrumentality thereof;

(4) Commerical paper that is rated "A" or better by a nationally recognized rating service: *Provided,* That any conflict in a rating shall be resolved in favor of the lower rating;

(5) Banker's acceptances that are payable by federally or State chartered banks that have executed a valid waiver of offset agreement: *Provided,* That the maturity of any given acceptance is not greater than 180 days and;

(6) State, county or municipal obligations that are rated "A" or better by a nationally recognized rating service: *Provided.* That any conflict in a rating shall be resolved in favor of the lower rating;

(7) Obligations of the Asian Development Bank, Inter-American Development Bank and the International Bank for Reconstruction and Development; or

(8) Any asset determined by the FDIC to be acceptable.

(e) *Deposit agreement.* A foreign bank shall not deposit any pledged asset required under § 346.19(c) until a deposit agreement acceptable to the FDIC has been executed. The agreement, in addition to other terms not inconsistent with this paragraph (e), shall give effect to the following terms:

(1) *Assets to be held for safekeeping.* The depository shall hold any asset deposited by the foreign bank pursuant to the deposit agreement for safekeeping as a special deposit free of any lien, charge, right of set-off, credit or preference in connection with any claim of the depository against the foreign bank.

(2) *Depository to furnish receipt.* Whenever the foreign bank deposits any assets, the depository shall provide the foreign bank with a receipt and shall provide the FDIC with a copy thereof. The receipt shall identify the deposit as having been made pursuant to the agreement under this section. The receipt shall specify, with respect to each asset or issue, the complete title, interest rate, series, serial number (if any), maturity date and call date. The foreign bank shall certify to the FDIC and the depository the lower of cost or market value for each asset and the aggregate of those values for all assets.

(3) *Examination of assets.* The depository shall hold any asset deposited by the foreign bank separate from all other assets and shall permit representatives of the foreign bank or the FDIC to examine the deposited assets.

(4) *List of pledged assets.* The depository shall furnish at the FDIC's request a written list of currently pledged assets. The list shall set forth information as requested by the FDIC.

(5) *Release of assets upon substitution of other assets.* (i) A depository shall release assets without the consent of the FDIC only in accordance with the provisions of this paragraph. The foreign bank shall, at the time of any release by the depository, deposit with the depository other assets of an aggregate value not less than the aggregate value of the assets released. The aggregate value of any assets deposited or released shall be based on the lower of cost or market value. The foreign bank shall certify to the depository that, after

giving effect to the exchange, the aggregate value of all assets remaining on deposit is at least equal to the amount required to be pledged under § 346.19(b). The certificate shall specify as to each asset released and each asset pledged: (A) The complete title; (B) the interest rate, series, serial number (if any), face value, maturity date, call date, the lower of cost or market value of each asset; and (C) the aggregate amount, based on cost or market value, whichever is lower, of assets. Upon receipt of the certificate and a statement by the foreign bank that a copy of the certificate is concurrently being furnished to the FDIC, the depository shall release assets.

(ii) The FDIC may suspend or terminate the right to exchange assets by written notice to the bank and the depository.

(6) *Release upon order of the FDIC.* The depository may release to the foreign bank any pledged asset upon the written order of the FDIC. The depository shall release only the assets specified in the order. The release of such assets may be made without pledging other assets, unless otherwise provided in the order.

(7) *Release to the FDIC.* Whenever the FDIC is obligated to pay insured deposits of an insured branch, the depository shall release to the FDIC any pledged asset upon the written certification of the FDIC that the FDIC has become so obligated. Upon receipt of certification and release of pledged assets, the depository shall be discharged from further obligation under the deposit agreement.

(8) *Interest earned on assets.* The foreign bank may receive any interest earned upon the pledged assets unless the depository receives an order by the FDIC prohibiting the receipt of interest.

(9) *Expenses of agreement.* The FDIC shall not be required to pay for any services under the agreement.

(10) *Termination of agreement.* The deposit agreement may be terminated by the foreign bank or the depository upon at least 60 days written notice to the other party. No termination shall be effective until (i) another depository has been designated by the foreign bank and approved by the FDIC; (ii) a deposit agreement acceptable to the FDIC has been agreed upon by the bank and the new depository; and (iii) the depository has released to the newly designated depository assets on deposit in accordance with the bank's written instructions, as approved by the FDIC.

(11) *Waiver of terms.* The FDIC may by written order relieve the foreign bank or the depository from compliance with any term or condition of the agreement.

(f) Each insured branch shall separately comply with the requirements of this section.

(g) In lieu of or in addition to a pledge of assets, a foreign bank may, with the approval of the FDIC, secure a surety bond for the benefit of the FDIC. The FDIC may set such terms and conditions for the surety bond as it deems necessary.

(h) *Exception.* Unless otherwise required by the FDIC, a bank organized under the laws of Pureto Rico, Guam, American Samoa or the Virgin Islands which is an insured bank other than by reason of having an insured branch, shall not be required to pledge assets under this section.

§ 346.20 Asset maintenance.

(a) An insured branch shall maintain on an average daily basis for the weekly computation period eligible assets that are payable in United States dollars (or in currency freely convertible to United States dollars) in an amount at least equal in book value to the amount of the branch's liabilities. In determining the eligible assets for the purposes of this section, the branch shall exclude (1) all amounts due from the parent bank and any other branch, agency, office or wholly owned subsidiary of the bank; (2) 50 percent or more of any asset classified "Doubtful" and 100 percent of any asset classified "Loss" in the most recent examination report prepared by the FDIC or the Comptroller of the Currency; and (3) any deposit of the branch in a bank unless the bank has executed a valid waiver of offset agreement. An asset not in the branch's actual possession shall be an eligible asset only if the branch holds title to such asset and the branch maintains records sufficient to enable independent verification of the branch's ownership of the asset. In determining the amount of liabilities, the branch shall exclude any amount due to the parent bank and any other branch, agency, office or wholly owned subsidiary of the bank.

(b) The average daily book value of the branch's assets and liabilities shall be computed at the close of the business every Wednesday for the preceding week. The branch may rely on this average value for the purpose of determining compliance with paragraph (a) of this section. Calculations as to the average daily value of the branch's assets and liabilities shall be retained by the branch until the next examination.

§ 346.21 Deductions from the assessment base.

An insured branch may deduct from it assessment base deposits in the insured branch of any office, branch or agency of and any wholly owned (except for a nominal number of director's shares) subsidiary.

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SMALL BUSINESS ADMINISTRATION

[13 CFR Part 121]

Method of Determining Small Business Status for Small Business Administration Loan Assistance

AGENCY: Small Business Administration.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: This proposed rulemaking would consider changes in the present formula method for determining a small business for the purposes of an SBA loan when the applicant has external operating affiliates. The present formula method has often been criticized as being unduly restrictive and unclear as to when its use is appropriate. The SBA hopes to clarify the method used to determine the status of applicants for SBA financial assistance.

DATE: Written comments must be submitted by May 23, 1979.

ADDRESS: Send all comments to: Kaleel C. Skeirik, Director, Size Standards Division, Small Business Administration, 1441 L Street, NW., Washington, D.C. 20416.

FOR FURTHER INFORMATION CONTACT: Robert N. Ray, (202) 653-6373

SUPPLEMENTARY INFORMATION: The general rule for determining the applicable size standard for loans where a concern operates in more than one industry, or has internal operating affiliates which operate in more than one industry, is to determine the primary industry and apply the size standard for that industry.

Currently, there is a special rule that applies when there are external-operating affiliates engaged in industries subject to different size standards. This rule begins as a part of the first paragraph of § 121.3-10 of the Small Business Size Standards and reads as follows:

If an applicant for an SBA loan has external-operating affiliates (i.e., affiliates which are primarily engaged in selling to the general public or to concerns other than the applicant concern or an affiliate thereof) and such external-operating affiliates are engaged