Banking

COMMISSION
OF THE EUROPEAN
COMMUNITIES

Brussels, 29/4-91

Office of SIR LEON BRITTAN

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FROM: Martin DONNELLY. telph.: 236.33.38
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TO: MR VAN ART, EC DELEGATION WASH.

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THE RIGHT HONOURABLE

SIR LEON BRITTAN, QC

VICE-PRESIDENT OF THE COMMISSION
OF THE EUROPEAN COMMUNITIES

RUE DE LA LOI, 200
1049 BRUSSELS - TEL. 235 25 14
235 26 10

30-04-1991

D'Amato,

Now that the House Banking Committee Sub-Committee on financial institutions has begun to hold hearings on the Financial Institutions Safety and Consumer Choice Bill you may find it helpful to have my preliminary reactions, as seen from the Commission of the European Communities, to the main aspects of the proposals as they are likely to affect European Community banks.

First let me express my strong support for the liberalising objectives of these proposals. The Commission has long emphasized the need for the removal of the restrictions on the geographical expansion of banks imposed by McFadden Act and the Douglas Amendment of the Bank Holding Company Act, and the strict limitations on the range of financial activities which banking organizations may carry out imposed by the Glass-Steagall Act and the Bank Holding Company Act. Their removal, as now proposed, would be a very positive step. It would increase business opportunities across the financial sector, enlarge consumer choice and be good for both the US and the world economy.

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The Honorable Frank Annunzio
Chairman,
Subcommittee on Financial Institutions,
Supervision, Regulation and Insurance
House of Representatives
Room 212 O'Neill House Office Building
WASHINGTON DC 20515
USA

This policy of opening up our financial markets is reinforced by the offer which the Community has made in the Uruguay Round negotiations on financial services to accept the right of our partners to establish or expand a commercial presence in the Community. This is defined to include branches as well as subsidiaries and other forms of establishment. It is my understanding that the United States is willing to make the same commitment.

Both the EC legislation I have described and the US Treasury's proposals aim at the same objectives of removing unnecessary limitations on bank powers as well as on geographic expansion. As indicated above, the Community has opted for the most liberal regulatory structure under which banks are allowed to carry out traditional deposit taking and lending activities and to engage in securities transactions under the same roof. This is an approach which we believe is both prudentially sound and economically efficient.

I appreciate that the proposed US legislation does not seek to go so far and instead would require the creation of specialized and separately capitalized subsidiaries to carry out different kinds of financial business. Even if it is accepted that this approach is to be adopted, at least at present, we are concerned that certain features in the detail of the proposals seriously detract from their generally positive character - to the detriment not only of foreign banks but also the competitive environment of US financial markets.

First, if a foreign bank wishes to engage in securities or insurance activities as well as traditional banking activities in the United States, it would no longer be permitted to conduct banking activities in the United States through branches or agencies. Existing branches and agencies of such foreign banks would have to be converted to a commercial bank subsidiary of a financial services holding company (FSHC).

The necessity of operating through a subsidiary bank would severely limit the ability of EC banks to compete effectively in the US market in the way they are permitted to do at present. For a foreign bank, the importance of being able to operate through a branch or agency is that its US banking activities can be conducted on the basis of the bank's consolidated worldwide capital, with US legal lending limits for the branch or agency calculated accordingly. If, however, a foreign bank were compelled to operate through a subsidiary, it would have to conduct its US banking activities on the basis of the capital of the US-incorporated subsidiary alone.

We therefore urge that foreign banks that wish to conduct securities and insurance activities in the United States be permitted to continue to conduct a traditional banking business in the United States through branches and agencies. As far as I am aware no prudential problems have arisen through this being permitted in the past, and the regulatory authorities have been well able to satisfy themselves as to the financial position of the foreign bank seeking to carry on business through branches or agencies in the US.

On the other hand under the structure as proposed, it would be reasonable to require foreign banks to conduct their securities and insurance activities through separately incorporated US subsidiaries.

This approach would also address our second point of concern with the Treasury proposal, namely, the requirement that foreign banks create an FSHC in the United States in order to establish securities or insurance subsidiaries. This would be a significant additional administrative burden implying increased operating costs. Moreover, an FSHC would be unnecessary on prudential grounds because the foreign parent bank would in any event be subject to the Financial Services Holding Company Act, and establishment and operation of securities and insurance subsidiaries would therefore be subject to approval and supervision by the appropriate US federal banking regulator as well as the appropriate US functional regulator. Banking operations in the United States would, in any case, continue to be subject to the approval and supervision of US banking regulators. What I am suggesting here does not involve more favourable treatment for foreign banks than for US banks, as I see no reason why the concerns about non-banking activities should not be met by requiring foreign as well as US banks to operate their non-banking activities through separately incorporated subsidiaries, but not necessarily by creating a new FSHC. Such an approach would meet the legitimate concerns that have been expressed, in a simpler and less cumbersome fashion. I understand this alternative has considerable support in responsible quarters within the US itself.

Finally, we note that the Treasury intends to impose capital standards higher than the minimum standards agreed in the Basle Committee of Banking Regulations and Supervisory Practices on US incorporated banks that wish to provide securities or insurance services through subsidiaries of an FSHC. We do not question the right of the US authorities to do this, but we do consider that any attempt to impose higher standards on foreign parent banks as a condition of establishing or operating a branch or agency in the United States would be inconsistent with efforts being made by international banking authorities—including US authorities—to facilitate the international activities of banks. The regulators of any non-banking subsidiary or affiliate would be able to satisfy themselves as to the capital adequacy of that concern, while the capital adequacy of the parent bank would be assured by its compliance with the internationally agreed standards.

I hope that you will feel able to encourage members of your Committee to consider very seriously whether the objectives of the Treasury's proposals can be met more effectively for foreign banks by the alternative structure I have outlined on these various points. We will of course be continuing our analysis of the proposals, and consulting further with representatives of the European industry. I therefore look forward to staying in touch with you on these important issues.

I am writing in similar terms to Henry Gonzalez, and to Don Riegle in the Senate as well as to Nicholas Brady and Alan Greenspan.

THE RIGHT HONOURABLE

SIR LEON BRITTAN, QC

VICE-PRESIDENT OF THE COMMISSION
OF THE EUROPEAN COMMUNITIES

RUE DE LA LOI 200
1049 BRUSSELS - TEL. 235 25 14
235 26 10

30-04-1991

Dear Mr Gonzalez,

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The Honorable Henry B GONZALEZ
Chairman, Committee on Banking, Finance
and Urban Affairs
House of Representatives
2413 Rayburn House Office Building
WASHINGTON DC 20515 - 4320
USA

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Yours sincerely

THE RIGHT HONOURABLE
SIR LEON BRITTAN, QC
VICE-PRESIDENT OF THE COMMISSION
OF THE EUROPEAN COMMUNITIES

RUE DE LA LOI 200
1049 BRUSSELS - TEL. 235 25 14
235 26 10

30-04-1991

Dear Mr Greenspan,

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First let me express my strong support for the liberalising objectives of these proposals. The Commission has long emphasized the need for the removal of the restrictions on the geographical expansion of banks imposed by McFadden Act and the Douglas Amendment of the Bank Holding Company Act, and the strict limitations on the range of financial activities which banking organizations may carry out imposed by the Glass-Steagall Act and the Bank Holding Company Act. Their removal, as now proposed, would be a very positive step. It would increase business opportunities across the financial sector, enlarge consumer choice and be good for both the US and the world economy.

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Alan GREENSPAN
Chairman,
Board of Governors of the
Federal Reserve System
WASHINGTON DC 20551
USA

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I was interested to note that in your recent testimony before the Senate Banking Committee you addressed, inter alia, the implications of the reform proposals on foreign banks. I look forward to staying in touch with you on these important issues.

I am writing in similar terms to Henry Gonzalez and Frank Annunzio in the House of Representatives, to Don Riegle in the Senate and to Nicholas Brady.

With good wishes.

Yours sincerely,

Leon Brittan

I read with great interest your own testimony on these matters.

THE RIGHT HONOURABLE
SIR LEON BRITTAN, QC
VICE-PRESIDENT OF THE COMMISSION
OF THE EUROPEAN COMMUNITIES

RUE DE LA LOI 200
1049 BRUSSELS - TEL. 235 25 14
235 26 10

30-04-1991

Dear Senator Riegle

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The Honorable Donald W RIEGLE Jr
Chairman,
Committee on Banking, Housing and
Urban Affairs,
US Senate
534 Dirksen Senate Office Building
WASHINGTON DC 20510
USA

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Yours sincerely,

Leon Brittan

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VICE-PRESIDENT OF THE COMMISSION
OF THE EUROPEAN COMMUNITIES

RUE DE LA LOI 200
1049 BRUSSELS - TEL. 235 25 14
235 26 10

30-04-1991

Dear Nick,

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First let me express my strong support for the liberalising objectives of these proposals. The Commission has long emphasized the need for the removal of the restrictions on the geographical expansion of banks imposed by McFadden Act and the Douglas Amendment of the Bank Holding Company Act, and the strict limitations on the range of financial activities which banking organizations may carry out imposed by the Glass-Steagall Act and the Bank Holding Company Act. Their removal, as now proposed, would be a very positive step. It would increase business opportunities across the financial sector, enlarge consumer choice and be good for both the US and the world economy.

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The Honorable Nicholas F. BRADY
Secretary of the Treasury
Department of the Treasury
Room 3330
15th and Pennsylvania Avenue,
NW, WASHINGTON DC 20220
USA

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This approach would also address our second point of concern with your proposals, namely, the requirement that foreign banks create an FSHC in the United States in order to establish securities or insurance subsidiaries. This would be a significant additional administrative burden implying increased operating costs. Moreover, an FSHC would be unnecessary on prudential grounds because the foreign parent bank would in any event be subject to the Financial Services Holding Company Act, and establishment and operation of securities and insurance subsidiaries would therefore be subject to approval and supervision by the appropriate US federal banking regulator as well as the appropriate US functional regulator. Banking operations in the United States would, in any case, continue to be subject to the approval and supervision of US banking regulators. What I am suggesting here does not involve more favourable treatment for foreign banks than for US banks, as I see no reason why the concerns about non-banking activities should not be met by requiring foreign as well as US banks to operate their non-banking activities through separately incorporated subsidiaries, but not necessarily by creating a new FSHC. Such an approach would meet the legitimate concerns that have been expressed, in a simpler and less cumbersome fashion. I understand this alternative has considerable support in responsible quarters within the US itself.

Finally, we note that the Treasury intends to impose capital standards higher than the minimum standards agreed in the Basle Committee of Banking Regulations and Supervisory Practices on US incorporated banks that wish to provide securities or insurance services through subsidiaries of an FSHC. We do not question the right of the US authorities to do this, but we do consider that any attempt to impose higher standards on foreign parent banks as a condition of establishing or operating a branch or agency in the United States would be inconsistent with efforts being made by international banking authorities—including US authorities—to facilitate the international activities of banks. The regulators of any non-banking subsidiary or affiliate would be able to satisfy themselves as to the capital adequacy of that concern, while the capital adequacy of the parent bank would be assured by its compliance with the internationally agreed standards.

I hope that you will feel able to consider very seriously whether the objectives of your proposals can be met more effectively for foreign banks by the alternative structure I have outlined on these various points. We will of course be continuing our analysis of the proposals, and consulting further with representatives of the European industry. I therefore look forward to staying in touch with you on these important issues.

I am writing in similar terms to Henry Gonzalez, and Frank Annunzio in the House of Representatives, to Don Riegle in the Senate and to Alan Greenspan.