The Regulation of Interstate Bank Branching Under the International Banking Act of 1978: The Stevenson Compromise

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In recent years observers have noted a remarkable flow of capital into the United States; foreign investment has almost quadrupled within the last decade. A segment of the economy in which foreign penetration is dramatically evident is the American banking industry. From 1973 to 1978 the U.S. holdings of foreign banks increased nearly 300%, from $24.6 billion to $96.1 billion. This compares with a 64% increase in the assets of domestic banks. In New York and California, where 90% of all foreign bank assets in the United States are held, foreign banks accounted in 1978 for 43 and 35%, respectively, of the total outstanding commercial and industrial loans. In 1972 there were 52 foreign banks with offices in the United States, and by November 1978 there were 129.

The increased foreign presence in the American banking industry results from general systemic changes within the international money markets, such as the development of the market for Euro-dollars.

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1 See, e.g., Investment Inflow: Foreign Stake in U.S. Rises but is Dwarfed by U.S. Stake Abroad, Wall St. J., July 3, 1978, at 1, col. 6; The Buying of America, NEWSWEEK, Nov. 27, 1978, at 78.
2 The Buying of America, supra note 1, at 81. The inflow of funds has been attributed to many factors, but it is generally ascribed to a faith held by foreigners in the basic political and economic stability of the United States and to their desire to capture a greater share of the large American market. See Investment Inflow: Foreign Stake in U.S. Rises but is Dwarfed by U.S. Stake Abroad, supra note 1, at 1, col. 6.
3 Here Come Foreign Banks Again, BUS. WEEK, June 26, 1978, at 78.
4 Id.
6 The Buying of America, supra note 1, at 88.
7 Gruber, Foreign Banks Still Boom, Chi. Tribune, Feb. 4, 1979, § 5, at 1, col. 3.
8 The Federal Reserve Board lists several of the important developmental factors as: The increase—more than fourfold—in the size of the Euro-dollar market since 1970 and, generally, the use of the U.S. dollar as a vehicle for international transactions have spurred banks in major industrial countries to establish a presence in the United States in order to clear the progressively larger volume of dollar transactions generated by their expanding international activities, to manage their liquidity positions, and to take advantage of arbitrage opportunities in international money markets.

Foreign banks have also established U.S. offices to finance trade and working capital needs and to provide foreign exchange, payments, and other corporate services for large home-country corporations that have invested in the United States. These investments have increased significantly since 1971. In addition, foreign banks compete with U.S. banks in
However, the marked increase of foreign banks in recent years can be attributed in part to an awareness that federal control of foreign banking in the United States was imminent. By expanding their operations before the passage of federal legislation, foreign bankers hoped to take advantage of expected grandfather clauses which would ensure the continued existence of established offices. In the fall of 1978, the federal control that had been anticipated finally materialized. The International Banking Act of 1978 (IBA), the first comprehensive regulation of foreign banks at the federal level, was signed into law. State-chartered foreign banks, as well as those which elect the newly provided option of federal chartering, were made subject to the provisions of the IBA.

Prior to the International Banking Act foreign bank activity was regulated by the individual states, rather than the federal government. Foreign banks’ freedom from federal control gave them certain competitive advantages over domestic banks. For example, foreign banks were not required to hold reserves at the Federal Reserve or to purchase insurance from the Federal Deposit Insurance Corporation. Furthermore, foreign banks were permitted to open branches in more than one state, a privilege denied domestic banks. Before the proliferation of foreign banks in the American market, the advantages held by foreign institutions created only a slight competitive disparity between domestic and foreign banks. When the competitive disparity widened because of the significant increase in foreign bank activity, federal legislators responded with the IBA.

financing trade of U.S. businesses with their home countries and in meeting the needs of multinational companies.


10 See Foreign Banks Gain Time for Expansion, supra note 9, at 36.


12 The federal government could, through indirect means, affect a small portion of the American operations of foreign banks, but the primary regulation of their activities fell to those individual states which permitted foreign banks to operate in their financial markets. For a comprehensive examination of pre-IBA regulatory policy, see Halperin, The Regulation of Foreign Banks in the United States, 9 INT’L LAW. 661 (1975).

13 See generally The Buying of America, supra note 1, at 82. See also note 64 infra.


15 Halperin, supra note 12, at 686.
The framers of the IBA regarded the foreign institutions' ability to branch interstate as the "single most controversial aspect of [foreign bank] operations in the United States." Of the proposed restrictions in the IBA, limits upon interstate branching were viewed as the most important. Powerful interests were aligned for and against federal regulatory control of foreign bank interstate branching.

The statutory provisions that emerged from this controversy attempt to address the concerns of both proponents and opponents of regulation. It is this deft compromise, developed by Senator Adlai Stevenson, which is the focus of this comment. The general history of the international banking legislation and positions supporting and opposing the regulation of interstate branching will be discussed. Thereafter, the elements of the Stevenson compromise will be explained and their efficacy illustrated. Finally, the current and potential effects of the compromise upon the entire banking system will be explored.

The Development of Federal Regulation of Foreign Banks

The first congressional study of foreign bank activity in the United States was undertaken in 1966. Subsequently several bills for the regulation of foreign banking were introduced, but all died in committee. Legislative activity heightened after the proposals of the Federal Reserve Steering Committee on International Banking were submitted to Congress in 1974. International banking legislation was introduced each successive year. In April 1978 the International Banking Act of 1978 was passed by the House of Representatives. In August the Senate approved the bill after making extensive revisions and the

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18 Adlai E. Stevenson III is the Junior Senator, Democrat, from Illinois. Senator Stevenson proposed the central provision, § 5, of the compromise on interstate branching. Section 14, proposed by Senator H. John Heinz III, became an adjunct to the central provision and for the purposes of this comment will be included in the discussion of the Stevenson compromise.
Senate version was adopted by the House. President Carter signed the IBA into law on September 17, 1978.

During the evolution of the IBA, the elimination of foreign banks from the domestic market was not seriously considered. The foreign presence in the United States banking industry has been recognized as beneficial to the American public. The IBA does not attempt to exclude foreign institutions; it was designed to equalize the competitive postures of domestic and foreign banks. The goal of the framers was to establish parity of treatment, clearly placing the focus of the regulations upon the enhancement of competition. The reception accorded the IBA in the international banking community suggests that the goal was achieved. Lord O'Brien, President of the British Bankers' Association and former Governor of the Bank of England, has commented that "the new Act is in general not unreasonable in its provisions and gives the promise of stable conditions for the foreseeable future." To achieve parity the IBA extends to foreign banks the ability to acquire nationally chartered banks or to charter their own national banks, to establish Edge Act corporations, and to obtain insurance...
through the Federal Deposit Insurance Corporation.\(^{35}\) Foreign banks are, however, now subject to the reserve requirements of the Federal Reserve Board\(^{36}\) and to the restrictions of the Bank Holding Company Act.\(^{37}\) Additionally, foreign banks are now restricted in their ability to establish branches in more than one state.\(^{38}\)

Among the IBA's provisions, none were so hotly contested or so subject to change as those dealing with interstate branching. During 1977 and 1978, four revised versions of section 5 were considered by Congress. The first was part of the proposed 1977 Act and prohibited interstate branching by federal or state branches of foreign banks until such time as national banks were extended the same privilege.\(^{39}\) This strong regulatory stance was reversed in the second version of section 5,\(^{40}\) the version eventually passed by the House.\(^{41}\) Under the second, foreign banks which had elected to federally charter their operations were not allowed to branch interstate because of the prohibition contained in the McFadden Act.\(^{42}\) State-chartered foreign institutions

\(^{34}\) The Edge Act, 12 U.S.C. §§ 611-632 (1970), provides domestic banks with the opportunity to establish corporations throughout the United States, to finance international trade and business. These corporations cannot enter into domestic banking, and can only accept those deposits incidental to the international transactions they facilitate. Section 3 of the IBA amends the Edge Act, allowing foreign banks to own Edge corporations and liberalizing the regulations on all such operations. See Senate Report, supra note 16, at 3-6.

\(^{35}\) Section 6 of the IBA, amending scattered sections of 12 U.S.C., allows foreign bank branches to obtain insurance from the Federal Deposit Insurance Corporation (FDIC). If, however, the foreign bank accepts deposits of less than $100,000 and the branch is federally-chartered or chartered in a state which requires deposit insurance of its domestic banks, then FDIC coverage is mandatory. See Senate Report, supra note 16, at 12-14.

\(^{36}\) The Federal Reserve Board's powers to set reserve requirements are extended by § 7 of the IBA, amending scattered sections of 12 U.S.C. The Federal Reserve can now set reserve requirements upon federally-chartered foreign branches and agencies, and also upon state-chartered branches and agencies of foreign institutions with worldwide consolidated bank assets in excess of $1,000,000,000. Sections 6, 7, 11, and 13 provide for the framework of federal supervision and examination of foreign bank activity in the United States. See Senate Report, supra note 16, at 13-14.

\(^{37}\) The Bank Holding Company Act (BHCA), 12 U.S.C. §§ 1841-1850 (1970), provides for the approval and complete supervision of the Federal Reserve Board for the non-bank activities and enterprises conducted directly or indirectly by domestic banks. Section 8 of the IBA amends the BHCA by subjecting foreign banking institutions to these same restrictions. The provision does include, however, a liberal grandfather clause which permits the continued existence, some temporarily and some permanently, of the non-bank activities which are not permissible under the BHCA. See Senate Report, supra note 16, at 14-17.

\(^{38}\) See notes 101-07 and accompanying text infra.

\(^{39}\) International Banking Act of 1977, supra note 22, at § 5.


\(^{42}\) H.R. 10899, supra note 40, at § 5.
were permitted to continue branching into those states allowing it.\textsuperscript{43} This mild version would not have significantly altered the prevailing regulatory framework or restricted foreign banks in their interstate branching.\textsuperscript{44} It is likely that foreign banks would have forgone federal chartering rather than be precluded from the opportunity to branch interstate.\textsuperscript{45} A third version, amending the provisions of the second, was proposed,\textsuperscript{46} but rejected,\textsuperscript{47} in the House. The amendment would have required, in addition to the approval of state banking regulators, explicit statutory authorization for interstate branching by state-chartered branches of foreign banks.\textsuperscript{48} The Senate Committee on Banking, Housing, and Urban Affairs, dissatisfied with the House-passed version, developed a fourth approach which became part of the final IBA.\textsuperscript{49} This revised section 5, suggested and championed by Senator Stevenson, was described by the Senator as a "means of skinning a couple of cats and still producing parity."\textsuperscript{50}

Essentially, section 5 of the Stevenson compromise permits interstate branching by foreign banks into those states expressly allowing their presence, but places certain limitations on the ability of the branches to accept deposits. Outside their home states,\textsuperscript{51} foreign bank branches may accept only those deposits incidental to the international transactions they facilitate.\textsuperscript{52} Section 5 also contains a grandfather clause which permits foreign bank branches already in existence to continue operations.\textsuperscript{53} Section 14 mandates that a study be prepared and be submitted to Congress on possible revisions of the McFadden Act.\textsuperscript{54} These provisions of the Stevenson compromise have muted the debate which once polarized the entire banking community.\textsuperscript{55}

\section*{The Foreign Bank Interstate Branching Controversy}

A variety of persons, organizations, and institutions took sides in

\begin{footnotes}
\item\textsuperscript{43} Id.
\item\textsuperscript{44} See House Passes Bill to Control Branches of Foreign Banks, supra note 17, at 3, col. 2.
\item\textsuperscript{45} Id.
\item\textsuperscript{47} 124 Cong. Rec. H2571 (daily ed. Apr. 6, 1978).
\item\textsuperscript{48} \textit{House Report}, supra note 46, at 1-2.
\item\textsuperscript{49} Pub. L. No. 95-369, supra note 11, at § 5.
\item\textsuperscript{50} Senate Hearing, supra note 28, at 72 (question of Sen. Stevenson).
\item\textsuperscript{51} See notes 106-07 and accompanying text \textit{infra}.
\item\textsuperscript{52} See notes 101-04 and accompanying text \textit{infra}.
\item\textsuperscript{53} See note 105 and accompanying text \textit{infra}.
\item\textsuperscript{54} See note 108 and accompanying text \textit{infra}.
\item\textsuperscript{55} Ganoe, \textit{How the Rules Changed for American Banking, Euromoney}, Nov. 1978, at 135.
\end{footnotes}
the heated controversy surrounding the regulation of interstate branching by foreign banks. Principal supporters of national restrictions were federal banking regulators and regional American bankers. An unusual coalition formed the opposition. As the natural objects of the legislation, foreign banks with current or planned investments in the United States were, as a matter of course, opposed to the proposed regulations. Aligning themselves with the foreign bankers, however, were state banking regulators who represented the interests of the individual states and the large American-based multinational banks. In spite of their unlikely association and their disparate reasons, all three groups supported the continuation of the status quo and fought to eliminate, or at least dilute, the proposed restrictions on interstate branching.

Federal banking regulators—primarily the Federal Reserve Board, the Department of the Treasury, and the Comptroller of the Currency—relied on the notion of national treatment as a theoretical basis for the federal regulation of foreign banks. When foreign businesses are afforded national treatment they are allowed to function much as domestic firms do, enjoying the comparable advantages and suffering the comparable restraints. Since domestic banks are restricted in their ability to branch interstate, it was strenuously argued that foreign banks "should play by our rules—even if the rules are not thoroughly satisfactory.” To reinforce the argument for national treatment of foreign banks, advocates of regulation emphasized that the United States was virtually the only country in the world in which neither the central government nor the central bank regulated the activities of foreign banks.

The support of regional American bankers for restricting foreign bank activities was based upon a fear of further foreign expansion into the domestic market. Regional bankers pointed out that the ability to branch interstate had allowed foreign banks to capitalize on their

56 See note 12 supra.
57 See notes 39-54 and accompanying text supra.
58 E.g., Senate Hearing, supra note 28, at 7 (statement of G. William Miller, Chairman, Federal Reserve Board), 64 (statement of Robert H. Mundheim, General Counsel, Department of the Treasury), 88 (statement of John G. Heimann, Comptroller of the Currency).
59 Id. at 64 (statement of Robert H. Mundheim).
60 Note 15 supra.
61 Senate Hearing, supra note 28, at 88 (statement of John G. Heimann).
62 Terzakis, How to Regulate Foreign Banks?, BANKING, July 1976, at 74. Other commentators have suggested possible arguments for national, over state, regulation based upon the Commerce Clause or upon the supremacy of international treaties. See, e.g., Halperin, supra note 12, at 674-79.
63 Foreign Banks Gain Time for Expansion, supra note 9, at 36.
unique capabilities in regional markets and had already enabled foreign banks to make significant inroads into their territories. Although foreign competition had not yet seriously affected regional bankers, the advantages held by foreign banks were perceived as a ripening competitive threat. Foreign banks had begun to attract the type of domestic corporate client which had traditionally looked to regional banks for its financial needs. Regional banks were also threatened in the area of retail banking, where aggressive competition for deposits was foreseen.

The principal argument advanced by foreign banks in opposition to federal regulation of their activities was that foreign banks posed no real threat to domestic institutions. Foreign bankers asserted that their expansion into the American market did not result from regulatory advantages. Such advantages were regarded as largely theoretical, because the foreign presence was limited, for the most part, to only three states: New York, California, and Illinois. Furthermore, domestic banks engage in a large degree of interstate activity through loan production offices, Edge Act corporations, grandfathered in-

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64 In addition to interstate branching, regional bankers complained that the lack of reserve requirements and FDIC insurance payments had reduced costs to foreign banks, thereby reducing their loan rates. See The Buying of America, supra note 1, at 82; Dufey and Giddy, Eurobankers May Lose their Advantage over US Banks, Euromoney, Jan. 1978, at 102. Also, foreign banks are traditionally more highly leveraged and accustomed to lower profit margins and smaller spreads, thus making it possible to offer better rates than can domestic banks. See Adkins, Foreign Banking's U.S. Invasion, Dun's Rev., Feb. 1978, at 78. Foreign banks are also able to transfer funds from the parent to the U.S. affiliates, obviating the need to pay high prices for domestic funds. See Gruber, supra note 7, at 4, col. 2. See also Unequal Opportunity Lenders, Forbes, Aug. 21, 1978, at 34-35.
65 See Adkins, supra note 64, at 76.
66 Foreign Banks Gain Time for Expansion, supra note 9, at 36 (comments of Robert B. Palmer, Executive Vice President, Philadelphia National Bank).
67 This type of client was characterized as the smaller corporate borrower who was without access to the commercial paper market. Field, Biting into the Big Apple, Euromoney, June 1978, at 53.
68 See Halperin, supra note 12, at 663; Adkins, supra note 64, at 76. Deposits are zealously guarded by retail bankers, for they are regarded as the "raw material" of banking. Senate Hearing, supra note 28, at 155 (statement of Robert B. Palmer, President, Bankers' Association for Foreign Trade).
70 Id. See, e.g., Senate Hearing, supra note 28, at 186 (statement of Serge Bellanger, Vice President and Chairman, Legislative Committee, Institute of Foreign Bankers), 247-48 (statement of Peter Leslie for the Banking Federation of the European Community).
72 Loan production offices are operated by the large domestic banks, outside the states in which they are based, as sales offices for their loanable funds. Although no official contract sign-
terstate bank affiliates,\textsuperscript{74} and non-bank affiliates of bank holding companies.\textsuperscript{75} It was noted that thirteen of the largest American banks had 1,483 offices conducting banking-type business in 43 states, not including the states in which their operations were based.\textsuperscript{76} Given this level of interstate activity by domestics, foreign bankers argued that a restriction upon their interstate branching was not necessary to facilitate competitive equality.\textsuperscript{77}

The lobbying efforts of state branching authorities were considered the most powerful of those opposing the IBA.\textsuperscript{78} The state regulators exerted strong pressure to avoid federal interstate branching regulations which could hinder states interested in attracting foreign banks to their regional markets.\textsuperscript{79} E.D. Dunn, President of the Conference of State Bank Supervisors and Georgia Commissioner of Banking and Finance, stated: “The real question in the interstate branching issue is not competitive equality between foreign and domestic banks, but competitive equality among the states themselves.”\textsuperscript{80} Supporters of the regulators’ position that restrictive interstate branching regulation would reduce competition between regional financial markets and national money centers asserted that restrictions would confine all future foreign banking activity to the states where international financial centers were already established.\textsuperscript{81} Other states would be denied the opportunity to interest foreign institutions in their banking markets.\textsuperscript{82}

The large American banks with multinational operations joined the opposition to the federal regulation of interstate branching by foreign banks. American multinational bankers feared that restrictive national legislative action could trigger foreign retaliation.\textsuperscript{83} With U.S.

\textsuperscript{73} See note 34 supra.

\textsuperscript{74} Then-existing interstate subsidiaries of five foreign and seven domestic bank holding companies were permanently grandfathered by the Bank Holding Company Act of 1956. See Confine-

\textsuperscript{75} See note 37 supra.


\textsuperscript{77} See Guenther, \textit{Legislative Doldrums}, 126 BANKER 1143, 1145 (1976).

\textsuperscript{78} \textit{Competing in America}, \textit{ECONOMIST}, Mar. 4, 1978, special survey supplement at 52.

\textsuperscript{79} \textit{Foreign Banks Gain Time for Expansion}, supra note 9, at 35.

\textsuperscript{80} \textit{Senate Hearing}, supra note 28, at 144 (statement of E.D. Dunn).


\textsuperscript{82} Id.

\textsuperscript{83} See \textit{Competing in America}, supra note 78, at 52. The fears of American multinational bank-

\textsuperscript{ers were based upon the veiled and not-so-veiled threats of foreign bankers. See \textit{The Regulatory Environ-

\textsuperscript{ment: Killing the Golden Goose?}, EUROMONEY, Nov. 1978, at 52. Exemplifying the threat-
bank assets overseas about three times greater than those of foreign banks in the United States, American multinational bankers decided that they had more to lose from counter-restrictions placed upon them abroad than they had to gain from federal regulation of foreign bank activity in the U.S. American banks are not generally restricted to single regions in foreign countries which have permitted them access, although some nations demand reciprocal treatment before granting entry to a U.S. bank. For example, a foreign country may not permit a Kansas bank to open a branch within its country, unless its own banks may open a branch in Kansas. If restrictive branching limitations were passed at home, domestic multinationals feared reciprocal treatment would foreclose profitable banking opportunities abroad.

The American multinational bankers' second rationale for objecting to branching limitations reflected a domestic, rather than international, motive. The large U.S. banks hoped to utilize the growth of foreign interstate branching as a primary argument for permitting them also to cross state lines. American multinationals did not seek to restrict their foreign competitors; they sought to free themselves from regulation, so that they could meet the challenge of foreign bank competition. The expansion of foreign banks across state borders was considered to be the "opening wedge" through which domestic banks could secure the same privilege. The elimination of this wedge would weaken the large American banks' case for removing the limits upon their ability to branch interstate.

It is understandable that political forces were set in motion to put [foreign banks] on an equal footing with domestic banks, but the timing of the proposed measures creates a bad taste, as it happens when the one-way flow of US investment abroad is turning into a reciprocal two-way flow.

The International Banking Act [of 1976] is being proposed after US banks have successfully built their international organizations. The same opportunity may now be taken away from foreign banks in the US.

At present there may seem to be no fear of retaliation. But resentment and political counter-currents build up with time, and retaliation cannot be excluded if the intended legislation becomes too restrictive and goes beyond what is considered fair treatment.

Reimpell, supra note 71, at 61-62.

85 See Competing in America, supra note 78, at 52. See also Unequal Opportunity, supra note 27, at 20.
87 See Halperin, supra note 12, at 655-56, 672-74.
88 Competing in America, supra note 78, at 52.
89 Morse, Control of Multinational Banking Operations, BANKER, Aug. 1977, at 35.
90 Confinement of Domestic Banking in the United States, supra note 5, at 4.
91 Ganoe, supra note 55, at 135.
THE STEVENSON COMPROMISE

The reconciliation of divergent viewpoints achieved in the interstate branching provisions of the International Banking Act has been characterized as a "classic case of common sense compromise." Congress accommodated the concerns of interested parties and avoided producing the hardships envisioned in alternate courses of action. The Stevenson compromise afforded a workable and equitable solution to the hotly debated question of interstate branching by foreign banks.

The compromise actually provides few restrictions, for it speaks principally to the branch form of organization. Restrictions upon the subsidiary form of foreign bank expansion were already contained in the Bank Holding Company Act. The IBA reasserts the limits upon the subsidiary form, prohibiting the establishment of subsidiaries outside a foreign bank holding company's home state. The agency form of organization, under which foreign banks are statutorily limited in their ability to transfer customers' funds, is permitted continued utilization under the Act. However, a foreign bank may not maintain a federally-chartered agency in a state where it already has a federal branch or state branch or agency. Under the IBA, representative offices, the foreign banks' counterpart of domestic loan production offices, must now be registered with the Treasury Department.

Section 5(a) (1-4) of the IBA provides a new type of branching

92 Id. at 137.
93 For a discussion of the organizational options open to foreign banks, see Note, supra note 14, at 151-54. See also Halperin, supra note 12, at 663-65.
94 12 U.S.C. §§ 1841-1849 (1970). A subsidiary bank is owned and/or controlled by a bank holding company, and its purchase or establishment subjects the holding company and subsidiary bank to regulation by the Federal Reserve Board. See Halperin, supra note 12, at 664.
96 No deposits are accepted by agencies; only credit balances for loan customers may be maintained. See Note, supra note 14, at 152.
98 Id.
99 See note 72 supra.
100 Pub. L. No. 95-369, supra note 11, at § 10.
101 Sec. 5. (a) Except as provided by subsection (b), (1) no foreign bank may directly or indirectly establish and operate a Federal branch outside of its home State unless (A) its operation is expressly permitted by the State in which it is to be operated, and (B) the foreign bank shall enter into an agreement or undertaking with the Board to receive only such deposits at the place of operation of such Federal branch as would be permissible for a corporation organized under section 25(a) of the Federal Reserve Act under rules and regulations administered by the Board; (2) no foreign bank may directly or indirectly establish and operate a State branch outside of its home State unless (A) it is approved by the bank regulatory authority of the State in which such branch is to be operated, and (B) the foreign bank shall enter into an agreement or undertaking with the Board to receive only such deposits at the place of operation of such State branch as would be permissible for a corporation organized.
opportunity for foreign banks. Outside a bank's home state, the traditional form of branch organization in which a bank conducts full-service operations cannot be utilized. If a foreign bank obtains state and federal approval, it can establish a limited branch, however. Deposits other than those arising out of the international financial transactions facilitated by the limited branch are forbidden. The limitation on deposits parallels a similar provision contained in the Edge Act. Express approval of an admitting state, derived from appropriate state law, is mandatory for the entry of foreign branches.

In spite of the limitation on branching contained in the IBA, a grandfather clause, section 5(b), assures existing foreign branches the right to continue complete operations. Under section 5(c) a foreign bank may elect as its home state any state in which it has a branch, agency, subsidiary bank, or subsidiary commercial lending company. If it fails to elect a home state, the selection will be made by the Federal Reserve Board. The Senate Banking Committee instructed the Board to prevent manipulation of the home state selection process by foreign banks attempting to evade IBA restrictions.

Section 14 of the IBA mandates that the President shall submit within one year a report analyzing the present restrictions on interstate...
branching contained in the McFadden Act. The report is to examine both the effects of the McFadden Act restrictions upon the general financial, banking, and economic environment, and the likely effects of any recommended changes.

The Stevenson compromise produces the parity in treatment for domestic and foreign banks which the legislature was seeking. Foreign banks are provided interstate opportunities that are similar to those already exploited by large American banks. The limited branches provided for in section 5, in conjunction with the subsidiaries, agencies, and representative offices, allow foreign banks to pursue roughly the same activities as domestic banks engage in with their Edge Act corporations and loan production offices. Furthermore, foreign banks' existing interstate operations are liberally protected by the grandfather clause of the Stevenson compromise. Nonetheless, regional banks are immunized from the risk of losing their retail deposits to the bigger, more highly competitive foreign banks, since foreign bank limited branches cannot accept such deposits. State banking authorities are still permitted to attract foreign banks and their supplies of loanable funds to regional financial markets. The fear of multinational bankers that overly-restrictive legislation would produce retaliation against their affiliates abroad is dissipated by the fact that section 5 does not unreasonably discriminate against foreign banks. In addition, the multinational bankers' hopes for the liberalization of domestic regulations are preserved by Congress in section 14, which mandates a review of the McFadden Act.

The passage of the IBA has quieted the controversy surrounding the presence of foreign banks in the United States.109 Most American and foreign bankers have praised the legislation.110 The success of the IBA derives from the willingness of Congress to consider and accommodate the legitimate concerns of different interest groups in the U.S. banking community. It is apparent that the chief vehicle for this accommodation, the Stevenson compromise, achieves an equitable solution to the most immediate problems of competitive imbalance in American banking.

(b) The report required by subsection (a) shall be transmitted to the Congress not later than one year after the date of enactment of this Act.

109 Ganoe, supra note 55, at 135.
110 Gruber, supra note 7, at 1, col. 3.
THE IBA AND THE FUTURE OF INTERSTATE BRANCHING

Beneath the arguments for and against interstate branching by foreign banks rests the more fundamental controversy concerning interstate branching for all banking institutions in the United States. To stimulate congressional debate on this issue, section 14 of the International Banking Act orders a presidential review of the McFadden Act.111 This provision has been described as furnishing the IBA with an "importance far beyond its legislative purpose."112

The achievement of the stated goal of parity in treatment for foreign and domestic banks was a practical first step in the revision of banking regulations. The prohibitions now placed upon interstate branching by the Stevenson compromise avert the problem which would arise if foreign banks were allowed to continue to expand their interstate operations without limits, while the growth of domestic banks remained suppressed by the McFadden Act. Without the IBA and in the event of the continuation of the McFadden Act, the decision at some future date either to terminate the expanded operations of foreign banks or to deny domestic banks the same opportunities would have been exceedingly difficult.113 The purpose of the IBA is to equalize the competitive postures of participants in the banking system, not to maximize competition absolutely. The current competitive environment has been stabilized; additional improvement of competition in the banking industry awaits further congressional action.

The opponents of the McFadden Act view the restriction of interstate branching as anti-competitive. Senator Thomas McIntyre characterized the McFadden Act as "the real culprit . . . which was enacted over 50 years ago and whose ghost limits competition in our banking system."114 It is generally hypothesized that the repeal of the McFadden Act would foster a consolidation of most of the individual banks in the United States, concentrating the industry in a few giant national banks.115 This concentration is regarded by supporters as long overdue and as necessary to enable U.S. banks to successfully compete in the

111 Note 108 and accompanying text supra. The one-year presidential study was mandated, instead of a multi-year commission, for it was determined that this was the most expedient and effective means of securing recommendations and information necessary for legislative reform. See Senate Report, supra note 16, at 11.
112 Ganoe, supra note 55, at 135.
113 See Senate Hearing, supra note 28, at 68 (statement of Robert H. Mundheim, General Counsel, Department of the Treasury).
115 See Ganoe, supra note 55, at 137.
world market. Anticipated benefits accruing from concentration center upon reduced costs to customers and increased profits to bank shareholders. One speculative advantage is that a greater degree of banking sophistication would be channeled to regional markets through the expansion of large money center banks. It is possible that American export activity would increase as businesses availed themselves of the expertise of multinational bankers.

In addition to the argument that restrictions on interstate branching hinder competition, another argument has been raised against the McFadden Act. In testifying on the IBA, three highly-placed federal regulators argued that structural and technological changes in the banking industry and in the entire economic system have eroded the rationale for restrictions imposed over fifty years ago. Commentators have noted that the advancements in electronic funds transfer systems and the influx of foreign participation in the banking market undermine the validity of the McFadden Act.

An advocate of the McFadden Act's repeal described the current regulatory scheme in dramatic terms:

State boundaries confine growing banks like the constraining wires that inhibit the growth of bonsai trees, bending back a natural expansiveness so as to produce powerful but constricted individuals. . . .

. . . The narrow-minded defense of meaningless geographical restraints is backward-looking, costly, unimaginative and, in the long run, futile.

Section 14 of the International Banking Act ensures a review of the interstate branching prohibition. The adoption of the provision provides pressure for significant change. Within this element of the Stevenson compromise lies the potential for great transformation of the American banking system, for both domestic and foreign financial institutions.

Robert F. Van Patten, Jr.

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116 See generally Confinement of Domestic Banking in the United States, supra note 5, at 1-2.
117 Id.
118 Senate Hearing, supra note 28, at 9 (statement of G. William Miller, Chairman, Federal Reserve Board), 68 (statement of Robert H. Mundheim, General Counsel, Department of the Treasury), 88 (statement of John G. Heimann, Comptroller of the Currency).
121 Unequal Opportunity, supra note 27, at 19-20.