



# INTERNATIONAL BANKING FOCUS

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The Institute's mission is to help resolve the many special legislative, regulatory and tax issues confronting **internationally headquartered** financial institutions that engage in banking, securities and/or insurance activities in the United States.

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**INSTITUTE SUBMITS COMMENT LETTER TO BASEL COMMITTEE ON HOME-HOST COUNTRY INFORMATION SHARING**

The Institute submitted a comment letter on February 28th to the Basel Committee on Banking Supervision addressing their consultative paper on information sharing between home and host country supervisors under Basel II. Reflecting policy positions articulated in earlier Institute submissions as well as in the Institute's ongoing series of conference calls with Nicholas Le Pan, Chairman of the Basel Committee's Accord Implementation Group, our letter expresses strong support for the Committee's recognition of the primacy of the home country consolidated supervisor and avoidance of duplicative supervisory requirements that increase the implementation burden for international banks. (Institute submissions and related documents are available at [www.iib.org/member/Basel-Capital/](http://www.iib.org/member/Basel-Capital/).) The Institute will also submit a comment letter on proposed rules issued on March 30th by the federal bank regulatory agencies on U.S. implementation of Basel II. In addition, the Institute plans further discussions on these issues with both the U.S. banking regulators and with Chairman Le Pan of the AIG in upcoming meetings in late May and June.

**INSTITUTE COMMENTS ON PROPOSED RULE IMPLEMENTING ENHANCED DUE DILIGENCE REQUIREMENTS FOR CORRESPONDENT ACCOUNTS UNDER SECTION 312 OF THE USA PATRIOT ACT**

The Institute filed a comment letter on March 6th regarding FinCEN's re-proposed rule implementing the enhanced due diligences procedures that covered financial institutions are required to apply under Section 312 of the USA Patriot Act to correspondent accounts maintained for non-U.S. banks that are deemed to be high-risk under Section 312. (The submission and related documents are available at [www.iib.org/member/Anti-Money/](http://www.iib.org/member/Anti-Money/).)

The Institute's comment letter expresses our continued support for the exception that was included in FinCEN's original proposed rule exempting offshore booking locations of international banks that are subject to comprehensive consolidated supervision (as determined by the Federal Reserve Board) from Section 312's enhanced due diligence requirements. As previously reported, FinCEN's latest proposal does not include this exception, and instead would simply permit the CCS status of an offshore booking location's head office or parent bank to be a factor in a covered financial institution's risk assessment and its determination of how to implement the enhanced due diligence requirements. The Institute's comment letter urges FinCEN to adopt the CCS exception as originally proposed.

Because we believe the CCS exception was not only consistent with the policies underlying 312 but also an important limitation on the extraterritorial and potentially discriminatory effects of Section 312 on international banks, we would urge interested member banks to encourage their home country regulators to contact Treasury and FinCEN to express their support for the preservation of the CCS exception.

Separately, the Institute also participated in a joint comment letter by leading industry groups that generally expresses support for FinCEN's risk-based approach to implementing the enhanced due diligence requirements of Section 312 and seeks clarification of a number of issues.

**INSTITUTE TO HOLD CONFERENCE CALL WITH FinCEN ON POTENTIAL REPORTING REQUIREMENTS FOR CROSS-BORDER WIRE TRANSFERS**

The Institute and a working group of member bank representatives will hold a conference call in mid-April with officials at Treasury's Financial Crimes Enforcement Network to provide our collective comments on FinCEN's survey seeking information about the feasibility and impact of potential reporting requirements for cross-border wire transfers. The Institute held a preliminary conference call with FinCEN in early March on a draft version of the survey. (Institute memoranda and related documents are available at [www.iib.org/member/Anti-Money/](http://www.iib.org/member/Anti-Money/).)

**FEDERAL RESERVE AMENDS REGULATION K TO INCLUDE AML PROGRAM REQUIREMENTS**

The Federal Reserve Board has adopted a final rule amending Regulation K to specify that certain U.S. banking offices of international banks, as well as U.S. Edge and Agreement corporations, are required to maintain anti-money laundering programs under the Bank Secrecy Act. The Board's final rule requires that the AML program of affected U.S. banking offices be approved either by the international bank's board of directors or "by a delegee acting under the express authority of the board of directors to approve the Bank Secrecy Act compliance program." This represents a change from the Board's proposed rule on this subject, which would have required approval of the program by the international bank's board of directors. The Institute objected to this requirement and suggested instead that the rule permit approval by the U.S. banking office's senior management (See Institute's June 30, 2003 comment letter at [www.iib.org/6-30-03CL\\_Johnson.pdf](http://www.iib.org/6-30-03CL_Johnson.pdf).)

**INSTITUTE MEETS WITH TREASURY AND IRS CONCERNING THE IRS' PROPOSAL TO INCREASE THE 93% FIXED RATIO AND TO MAKE OTHER FAVORABLE CHANGES TO REGULATION SECTION 1.882-5**

On February 9th the Institute held a productive meeting with U.S. Treasury International Tax Counsel Hal Hicks and other Treasury and IRS representatives to discuss the proposed changes to Treasury regulation section 1.882-5 that were announced in Notice 2005-53, dealing with the determination of the deductible interest expense of a U.S. branch of an internationally headquartered bank. As previously reported, the Notice responds to a number of issues under regulation section 1.882-5 that the Institute has long advocated. The Institute's October 31, 2005 comment letter on the proposed changes is available at [www.iib.org/member/Interest-Expense/](http://www.iib.org/member/Interest-Expense/).

Most welcome is the IRS' indication that its review of recent data suggests that the 93% fixed ratio is too low. The meeting focused on data and other information that would support an increase of the fixed ratio to somewhere between 94 - 96% (and hopefully at the high end of this range), as well as the interface between the fixed ratio and treaty-based, risk-weighted allocations of interest expense.

The Institute also requested Treasury to issue guidance regarding other open issues under section 1.882-5, including the treatment of repos and other offsetting financial positions, derivatives, interbranch funding, and cross-border and cross-currency hedging activities, as well as guidance regarding the application of treaty-based, risk-weighted methods for allocating interest expense. Unfortunately, Treasury indicated that it is unable to provide guidance in these areas in the near future due to its time commitments to other pending projects.

**INSTITUTE CONTINUES DISCUSSIONS WITH TREASURY AND IRS ON PERMITTING USE OF IFRS IN CONNECTION WITH PROPOSED SAFE HARBOR FOR MARK-TO-MARKET SECURITIES VALUATIONS**

The Institute continues to make progress in our efforts to address concerns about the discriminatory treatment of internationally headquartered financial institutions under the recently issued proposed IRS regulations for valuing securities positions (including derivatives and currencies) for purposes of the "mark-to-market" rules of Internal Revenue Code section 475. The Institute had a productive meeting on February 9th with Treasury Associate Tax Legislative Counsel Michael Novey, IRS Associate Chief Counsel (Financial Institutions & Products) Lon Smith and their staffs. This was followed up by a letter to Treasury and the IRS succinctly setting forth our recommendations, and a further helpful exchange with Mr. Novey, International Tax Counsel Hal Hicks, and Associate International Tax Counsel Andrew Froberg, who participated on the tax panel during the Institute's Annual Washington Conference.

The proposed regulations would allow dealers (and electing traders) in securities, commodities and derivatives to treat the values of positions reported on certain financial statements as the fair market value of

those positions for purposes of the mark-to-market rules of section 475 (the “book/tax conformity safe harbor”). While the proposed book/tax conformity safe harbor is a welcome development, as currently proposed it will not be available to many U.S. branches of foreign banks and to foreign-based dealers in respect of their global dealing activities because it requires that those institutions have U.S. GAAP financial statements. This condition is NOT satisfied by those institutions that merely file with the SEC a reconciliation to U.S. GAAP, and therefore, nearly every major financial institution that books a portion of its global dealing positions outside its U.S. broker-dealer will face problems under the proposed regulations.

The Institute has been urging the IRS to address these problems, and has expressed concern that failure to extend the benefits of the safe harbor to foreign-based institutions would be inconsistent with “national treatment” principles that are intended to prevent discriminatory treatment of foreign-based institutions. We understand that the Treasury and IRS are seriously evaluating our proposals for addressing these problems, but that additional effort will be necessary to achieve a favorable outcome.

The Institute is working with members of the syndicate of institutions that have agreed to support this project. Other member institutions that wish to join the syndicate and participate in this effort should contact the Institute. (Institute memoranda, submissions and related documents on this issue are available in the member area of our web site at <http://www.iib.org/member/Other-Matters/>)