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OTS Authorizes Federal Savings Bank to Establish a Subsidiary Bank in China

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On December 6, 2007, the Office of Thrift Supervision (OTS) approved the application of GE Money Bank, a federal savings bank headquartered in Salt Lake City, Utah, to establish an operating subsidiary in the People's Republic of China that will initially engage in corporate lending, small business lending, and trade finance activities, and will subsequently become a full-service Chinese bank.

GE Money Bank is an indirect subsidiary of General Electric Capital Corporation (GE Capital), which in turn is a subsidiary of General Electric Company. The proposed operating subsidiary is currently a wholly owned dormant finance company subsidiary of GE Capital, organized under Chinese law and headquartered in Shanghai. In the proposed transaction, GE Money Bank will acquire all of the interests of the operating subsidiary, with the result that the operating subsidiary will become a wholly owned subsidiary of GE Money Bank. The operating subsidiary will change its name to "GE Capital Bank China."

It is anticipated that GE Capital Bank China will obtain necessary approvals from the Chinese government to become a full service Chinese bank, and will be permitted to engage in a full range of commercial and retail banking transactions in foreign and Chinese currency. The China Bank Regulatory Commission (CBRC) will supervise and examine GE Capital Bank as a Chinese bank. The CBRC and the OTS have established a structure to share supervisory information obtained from CBRC's examinations and monitoring of the new bank.

The OTS's approval was granted pursuant to the standard operating subsidiary application procedures set forth in 12 C.F.R. § 559.11. The OTS concluded that the activities of the operating subsidiary are permissible for federal savings banks. In its approval, the OTS cited a November 2000 Opinion of Chief Counsel establishing that federal savings banks may engage in foreign activities when those activities are otherwise permissible for a federal savings bank, can be conducted in a safe and sound manner, and are incidental to the clearly permissible activities of a federal savings bank. The OTS referred to further authority supporting the conclusion that the new bank's activities will be "incidental" to the parent U.S. savings bank's domestic operations because they will represent less than 5% of the U.S. savings bank's assets and revenues.

This approval is significant as a precedent for authorizing a U.S. federal savings bank to establish and operate a subsidiary bank outside of the United States. Federal banking laws long ago established the authority of national banks and other U.S. commercial banks to enter foreign banking markets. However, the federal Home Owners' Loan Act (HOLA), which governs federal savings banks, contains no explicit authority for federal savings banks to own foreign banks, consistent with the historical view of thrifts as domestic institutions created principally to facilitate home ownership in the United States.

In its GE Money Bank approval, the OTS staff acknowledged that HOLA does not explicitly authorize federal savings banks to engage in foreign activities, but concluded in effect that the statute's silence does not constitute a prohibition on foreign activities if they are otherwise permissible for a federal savings bank and the other conditions referenced above are satisfied. This approval should logically provide a basis under U.S. law for a federal savings bank to establish a subsidiary bank in any foreign jurisdiction so long as the OTS is satisfied that the subsidiary will be appropriately supervised and the other conditions set forth in the OTS approval are met.

More particularly, the approval appears to establish a route by which OTS-regulated savings institutions can participate in the fast-growing Chinese financial markets through their own wholly owned bank subsidiaries. This approval, if available to other savings institutions, appears at least partially to level the playing field between U.S. thrifts and commercial banks in their ability to enter the burgeoning Chinese bank market. The opening of this avenue for federal savings banks comes at an opportune time. In the wake of its accession to the World Trade Organization in 2001, China has been gradually opening its financial markets to the world in general, and has become more receptive to admitting U.S.-based financial institutions in particular.

The Chinese government has generally limited foreign investment in existing Chinese banks to 25%, with a 20% limitation on the amount any one investor can invest in any one bank. Under these rules, a number of U.S. banks, including Bank of America and Citibank, have recently taken significant minority positions in large Chinese banks.

Of more relevance to this discussion, however, the Chinese government in late 2006 clarified and liberalized the rules under which foreign banks can establish *de novo* wholly owned or joint-venture subsidiary banks in China without regard to the foreign 25% ownership restriction applicable to existing banks. In 2007, a number of non-Chinese banks, including Citibank, JPMorgan, United Overseas Bank (Singapore), Woori Bank (Korea), HSBC (U.K.), and Standard Chartered Bank (U.K.) have received approvals from the CBRC to establish subsidiaries under these new procedures, and many more banks are likely to follow in their footsteps.

Not surprisingly, the rules for establishing a foreign-owned subsidiary bank, which the Chinese government refers to as a “wholly foreign-funded bank,” impose a number of financial and prudential requirements. One requirement that would initially be difficult for many federal savings banks to meet is that the parent bank must have had a representative office in China for at least two years. Any federal savings bank interested in establishing a Chinese subsidiary bank should therefore consider establishing a representative office in China as soon as possible.

For its part, the United States banking regulators have recently begun to allow mainland Chinese banks to enter the U.S. markets after a 15-year effective moratorium based in part on concerns regarding the effectiveness of Chinese bank supervisory standards. In October 2007, the Federal Reserve Board approved the application of China Merchants Bank, a Chinese commercial bank, to open a New York branch. Also in October 2007, China Minsheng Banking Corp., another mainland Chinese bank, agreed to buy a 9.9% stake in UCBH Holdings, a San Francisco-based bank holding company that serves the Chinese-American community in California. Additionally, one of the largest government-sponsored Chinese banks, Industrial and Commercial Bank of China (ICBC), has an application pending with the U.S. regulators to open a branch in New York.