

A Bill for an Act Relating to International Banking Facilities.

Be It Enacted by the Legislature of the State of Hawaii:

SECTION 1. The legislature hereby declares that Hawaii has grown to be a leading center for international commerce and finance in the Pacific. In recent years, however, this leadership has been challenged, particularly in the field of international banking, where significant amounts of business activity is currently conducted in London, Hong Kong, the Caribbean, and other off-shore locations. Development of this off-shore business is due, in a large part, to federal regulatory requirements, and state and county taxes. Federal reserve system regulations prohibiting payment of interest on deposits of less than thirty days or requiring maintenance of reserves of bank deposits, reduced the incentive for United States banks to conduct international business in domestic locations.

In recent actions, however, the board of governors of the federal reserve system has amended Regulation D, "Reserve Requirements of Depository Institutions" (12 CFR Part 204) and Regulation Q, "Interest on Deposits" (12 CFR Part 217) to authorize beginning December 3, 1981, the establishment in the United States of international banking facilities (IBFs) by U.S. depository institutions, Edge or Agreement Corporations, and branches and agencies of foreign banks located in the United States. By December 22, 1981, there were 254 IBF's operating in the U.S., with the majority (135) in New York, and the rest scattered in 16 other states. Volume by the end of the year (only four weeks after the federal reserve action) totalled \$52 billion, with \$18 billion in New York IBF's and \$9 billion in other states.

Under the rules adopted by the board, an IBF may accept deposits from foreign residents (including banks), or from other IBFs. Such deposits are now exempt from reserve requirements of Regulation D and from interest rate limitations of Regulation Q. IBFs are now permitted to offer to foreign non-bank residents large denomination time deposits with a minimum maturity or required notice period prior to withdrawal of at least two business days. In addition, IBFs are permitted to offer overnight time deposits to foreign offices of U.S. depository institutions or foreign banks to other IBFs, foreign central banks, or to the institution establishing the IBF. Funds raised by the IBF can be used only to extend credit to foreign residents, to other IBFs, or to an institution establishing an IBF. Funds derived by an institution from its own IBF will be subject to Eurocurrency reserve requirements.

The legislature believes that the establishment of IBFs in U.S. banking offices will enhance the international competitive position of banking institutions located in the United States.

The legislature further finds and declares that banks pay much higher income taxes on foreign transactions conducted in Hawaii than would be paid in Hong Kong, London, or other off-shore locations and, therefore, continuation of taxes on this class of transactions when conducted in the State provides a strong incentive for banks to continue and expand their conduct of international transactions from foreign sites.

The legislature intends by the enactment of this Act to permit the establishment of Hawaii-based international banking facilities for the purpose of making loans to or accepting deposits from certain foreign customers, free from either investment interest rate restrictions or reserve requirements, as well as state and county taxes. Related foreign exchange transactions shall also be eligible. These provisions permit a domestic bank to make loans and accept deposits from specified foreign customers through their Hawaii-based international banking facility under essentially the same conditions which exist outside of the United States where the business is currently conducted.

The legislature further intends by enactment of this Act to provide for the exemption of income from an international banking facility from state and county taxation, subject to a tax floor provision to maintain revenues from international business which is currently conducted from Hawaii sites, and, therefore, taxable. The floor is to be phased out over a ten-year period, affording ample opportunity to further protect the revenue base in light of continuing assessment of the economic development impact of the creation of these facilities.

SECTION 2. The Hawaii Revised Statutes is amended by adding a new part to be appropriately designated and to read:

“PART . INTERNATIONAL BANKING FACILITIES

§ - **Definitions.** As used in this part:

- (1) “Bank” includes any organization subject to chapter 403 or 407.
- (2) “International banking facility” or “IBF” means a set of asset and liability accounts segregated on the books and records of a depository institution, United States branch or agency of a foreign bank, or an Edge or Agreement Corporation that includes only international banking facility time deposits and international banking facility extensions of credit.
- (3) “International banking facility extension of credit” or “IBF loan” means any transaction where an IBF supplies funds by making a loan, or placing funds in a deposit account. Such transactions may be represented by a promissory note, security, acknowledgement of advance, due bill, repurchase agreement, or any other form of credit transaction. Such credit may be extended only to:
 - (A) Any office located outside the United States of another depository institution organized under the laws of the United States or an Edge or Agreement Corporation;
 - (B) Any office located outside the United States of a foreign bank;
 - (C) A United States or a non-United States office of the institution establishing the IBF;
 - (D) Another IBF;
 - (E) An institution whose time deposits are exempt from interest rate limitations under section 217.3(g) of Regulation Q (12 CFR 217.3(g)) of the Board of Governors of the Federal Reserve System; or
 - (F) A non-United States resident or a foreign branch, office, subsidiary, affiliate, or other foreign establishment (“foreign affiliate”) controlled by one or more domestic corporations; provided that the funds are used

only to finance the operations outside the United States of the borrower or of its affiliates located outside the United States.

(4) "International banking facility time deposit" or "IBF time deposit" means a deposit, placement, borrowing, or similar obligation represented by a promissory note, acknowledgement of advance, or similar instrument that is not issued in negotiable or bearer form; and

(A) That must remain on deposit at the IBF at least overnight;

(B) That is issued to:

- (1) Any office located outside the United States of another depository institution organized under the laws of the United States or of an Edge or Agreement Corporation;
- (2) Any office located outside the United States of a foreign bank;
- (3) A United States office or a non-United States office of the entity establishing the IBF;
- (4) Another IBF; or
- (5) An institution whose time deposits are exempt from interest rate limitations under section 217.3(g) of Regulation Q (12 CFR 217.3(g)) of the Board of Governors of the Federal Reserve System;

(C) That is payable:

- (1) On a specified date not less than two business days after the date of deposit;
- (2) Upon expiration of a specified period of time not less than two business days after the date of deposit; or
- (3) Upon written notice that actually is required to be given by the depositor not less than two business days prior to the date of withdrawal;

(D) That represents funds deposited to the credit of a non-United States resident of a foreign branch, office, subsidiary, affiliate, or other foreign establishment ("foreign affiliate") controlled by one or more domestic corporations; provided that such funds are used only to support the operations outside the United States of the depositor or of its affiliates located outside the United States; and

(E) That is maintained under an agreement or arrangement under which no deposit or withdrawal of less than \$100,000 is permitted, except that a withdrawal of less than \$100,000 is permitted if such withdrawal closes an account.

§ - International banking facilities, establishment of; notice to bank examiner, quarterly reports. (a) Except for federal law, any other law to the contrary notwithstanding, any bank organized under chapter 403, or savings and loan association subject to chapter 407, may establish one or more international banking facilities for the purpose of:

- (1) Making, arranging for, placing, or servicing loans to foreign persons; provided that in the case of a foreign person which is an individual, or which is a foreign branch of a domestic corporation (other than a bank), or which is a foreign corporation or foreign partnership which is

eighty per cent or more owned or controlled, either directly or indirectly, by one or more domestic corporations (other than a bank), domestic partnership, or resident individual, all the proceeds of the loan shall be for use outside of the United States;

- (2) Making or placing deposits of foreign persons which are banks or foreign branches of banks (including foreign subsidiaries or foreign branches of the taxpayer) or with other international banking facilities;
- (3) Entering into foreign exchange trading or hedging transactions related to any other transactions described in this paragraph; and

(4) Accepting deposits from foreign persons.

(b) International banking facilities may be located in any county.

(c) At least fourteen days prior to the first reserve computation period that any institution intends to establish an international banking facility, the institution shall provide the bank examiner with a copy of the statement of intention required under Regulation D (12 CFR Part 204) of the Board of Governors of the Federal Reserve System.

(d) An institution which establishes an international banking facility shall provide the bank examiner with a copy of each quarterly report concerning the operations of its international banking facility which is required under Regulation D (12 CFR Part 204) of the Board of Governors of the Federal Reserve System.”

SECTION 3. Chapter 241, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read:

“§241- Deduction from entire net income. There shall be allowed as a deduction from entire net income to the extent not deductible in determining federal taxable income, the adjusted eligible net income of an international banking facility, as defined in chapter , part , determined as follows:

- (1) The eligible net income of an international banking facility shall be the amount remaining after subtracting from the eligible gross income the applicable expenses.
- (2) Eligible gross income shall be the gross income derived by an international banking facility from:
 - (A) Making, arranging for, placing, or servicing loans to foreign persons; provided that in the case of a foreign person which is an individual, or which is a foreign branch of a domestic corporation (other than a bank), or which is a foreign corporation or foreign partnership which is eighty per cent or more owned or controlled, either directly or indirectly, by one or more domestic corporations (other than a bank), domestic partnership, or resident individual, substantially all the proceeds of the loan shall be for use outside of the United States;
 - (B) Making or placing deposits with foreign persons which are banks or foreign branches of banks (including foreign subsidiaries or foreign branches of the taxpayer) or with other international banking facilities; or
 - (C) Entering into foreign exchange trading or hedging transactions related to any of the transactions described in this paragraph.

- (3) Applicable expenses shall be any expense or other deduction attributable, directly or indirectly, to the eligible gross income described in paragraph (2).
- (4) Adjusted eligible net income shall be determined by subtracting from eligible net income the ineligible funding amount, and by subtracting from the amount then remaining the floor amount.
- (5) The ineligible funding amount shall be the amount, if any, determined by multiplying eligible net income by a fraction, the numerator of which is the average aggregate amount for the taxable year of all liabilities, including deposits, and other sources of funds to the international banking facility which were not owed to or received from foreign persons, and the denominator of which is the average aggregate amount from the taxable year of all liabilities, including deposits and other sources of funds of the international banking facility.
- (6) The floor amount shall be the amount, if any, determined by multiplying the amount remaining after subtracting the ineligible funding amount from the eligible net income by a fraction, not greater than one, which is determined as follows:
 - (A) The numerator shall be:
 - (i) The percentage, as set forth in subparagraph (C), of the average aggregate amount of the taxpayer's loans to foreign persons and deposits with foreign persons which are banks or foreign branches of banks, or savings and loan associations or foreign branches of savings and loan associations, as the case may be, (including foreign subsidiaries or foreign branches of the taxpayer), which loans and deposits were recorded in the financial accounts of the taxpayer for its branches, agencies, and offices within the State for taxable years 1980, 1981, and 1982, minus;
 - (ii) The average aggregate amount of such loans and such deposits for the taxable year of the taxpayer (other than such loans and deposits to an international banking facility); provided that in no case shall the amount determined in this clause exceed the amount determined in this subparagraph; and
 - (B) The denominator shall be the average aggregate amount of the loans to foreign persons and deposits with foreign persons which are banks or foreign branches of banks, including foreign subsidiaries or foreign branches of the bank, (or savings and loan associations, as the case may be) which loans and deposits were recorded in the financial accounts of the taxpayer's international banking facility for the taxable year.
 - (C) The percentage shall be one hundred per cent for the first taxable year in which the taxpayer establishes an international banking facility and for the next succeeding four taxable years. The percentage shall be eighty per cent for the sixth, sixty per cent for the seventh, forty per cent for the eighth, and twenty per cent for

the ninth and tenth taxable years next succeeding the year such bank or savings and loan association establishes such facility, and zero in the eleventh succeeding year and thereafter.

- (7) If adjusted eligible net income is a loss, the amount of such loss shall be added to entire net income.
- (8) As used in this section, the term “foreign person” means:
 - (A) An individual who is not a resident of the United States,
 - (B) A foreign corporation, a foreign partnership, or a foreign trust, as defined in section 7701 of the federal Internal Revenue Code of 1954, as amended, other than a domestic branch thereof,
 - (C) A foreign branch of a domestic corporation (including the taxpayer),
 - (D) A foreign government or an international organization or an agency of either, or
 - (E) An international banking facility.

For the purposes of this paragraph, the term “foreign” and “domestic” have the same meaning as set forth in section 7701 of the federal Internal Revenue Code of 1954, as amended.”

SECTION 4. New statutory material is underscored.¹

SECTION 5. This Act shall take effect upon its approval.

(Approved June 14, 1983.)

Note

- 1. Edited pursuant to HRS §23G-16.5.