

May 9, 2012

## Federal Reserve Approves First Acquisition in the United States by a Chinese Bank

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### **Federal Reserve Makes First CCS Determination for a Chinese Bank in Approving the Acquisition of The Bank of East Asia (U.S.A.) National Association by Industrial and Commercial Bank of China Limited**

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On May 9, 2012, the Board of Governors of the Federal Reserve System (the “FRB”) issued an order (the “Order”) approving the acquisition of 80% of the shares of common stock of The Bank of East Asia (U.S.A.) National Association (“BEAUSA”), by Industrial and Commercial Bank of China Limited (“ICBC”).<sup>1</sup> This Order marks the first occasion on which the FRB approved the acquisition of a U.S. bank by a Chinese bank since the Bank Holding Company Act of 1956 (the “BHC Act”) was amended by the Foreign Bank Supervision Enhancement Act of 1991 (“FBSEA”). The FBSEA, which increased federal supervision of foreign banks operating in the United States, requires the FRB to make a finding that a foreign bank seeking to acquire control of a U.S. bank is subject to comprehensive supervision on a consolidated basis (“CCS”) by its home country supervisor. The Order marks the first time that the FRB has made a full and unqualified CCS determination for a Chinese bank to acquire control of a U.S. bank, although it has previously made a so-called “limited” CCS determination in the context of Chinese banks establishing U.S. branches.

On November 8, 2007, the FRB approved an application by China Merchants Bank Co., Ltd. (“CMB”) to establish a branch in New York, New York, the first such approval for a Chinese bank since the FBSEA. The FRB made a “limited” CCS determination pursuant to a provision that allows the FRB to approve a branch application if the appropriate authorities in the home country of the foreign bank are actively working to establish arrangements for the consolidated supervision of the bank submitting the application, and all other factors are consistent with approval. The FRB’s approval of CMB’s branch application opened the door for other Chinese banks to apply for branches in the United States. Thereafter, branch

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approvals based on similarly limited findings of CCS were granted by the FRB to ICBC in November of 2008 and to China Construction Bank Corporation in March of 2009. The “limited” CCS determination available for a branch application is not available for an application to acquire a U.S. bank under Section 3 of the BHC Act, which requires the FRB to make a full and unqualified CCS determination.

The FRB’s evaluation of whether ICBC is subject to CCS was foreshadowed in the FRB’s August 31, 2010 determination that CIC, an investment vehicle organized by the Chinese government, qualified under the CCS standard in the context of a Section 3 application for CIC’s *non-controlling*, but greater than 5%, investment in the shares of common stock of Morgan Stanley. The FRB explicitly noted, however, that that finding was based on both the unique nature and structure of CIC and the non-controlling nature of the investment under consideration in that application. In addition, the FRB noted that, in evaluating a proposal by a Chinese bank to acquire a U.S. bank, the FRB would evaluate whether that Chinese bank is subject to CCS.

In the Order, the FRB detailed its exhaustive analysis on the CCS of ICBC by the China Banking Regulatory Commission and other regulatory authorities including, among others, the People’s Bank of China, the State Administration of Foreign Exchange, China Securities Regulatory Commission and China Insurance Regulatory Commission. The Order also noted the International Monetary Fund’s most recent determination that China’s overall regulatory and supervisory framework adheres to international standards. In addition, the FRB noted China’s efforts on combating money laundering and terrorism financing and found that the anti-money laundering efforts by ICBC and the Chinese regulators are consistent with approval.

The Order should create the opportunity for other leading Chinese banks to acquire U.S. banks of a relatively modest size. Although the CCS determination is nominally bank-specific, in practice a CCS determination for one bank in a country is typically precedential for all similarly situated banks in that country. In addition, because the FRB takes the position that a CCS determination is required before a foreign banking organization can obtain financial holding company (“FHC”) status, the Order should pave the way for Chinese banks and their holding companies that are subject to the BHC Act to become FHCs.

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Sullivan & Cromwell LLP advised The Bank of East Asia, Limited on the sale of BEAUSA to ICBC, CMB on its branch application, CIC and Huijin in connection with ICBC's acquisition of BEAUSA, and CIC on its non-controlling investment in Morgan Stanley.

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### ENDNOTE(S)

- <sup>1</sup> The Order also approved the indirect acquisition of 80% of the shares of common stock of BEAUSA by China Investment Corporation ("CIC") and Central Huijin Investment Ltd. ("Huijin"). An application was necessary because CIC and Huijin are deemed to control ICBC.

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