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Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549-0609

17 October 2003

FAO: Jonathon G. Katz, Secretary

Re: Proposed Rule: Foreign Bank Exemption from the Insider Lending
Prohibition of Exchange Act Section 13(k) (File No. S7-15-03)

Ladies and Gentlemen:

We respectfully submit this letter in response to the request of the Securities and Exchange Commission (the "Commission") for comments on the Commission's proposed Rule 13k-1 (the "Proposed Rule"), as set forth in Release No. 34-48481 (the "Release"). The Proposed Rule would exempt qualified foreign banks from the insider lending prohibition of Section 13(k) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as added by Section 402 of the Sarbanes-Oxley Act. We appreciate this opportunity to comment on the Proposed Rule.

Headquartered in London, HSBC Holdings plc ("HSBC") is one of the world's largest banking and financial services organizations. Its international network comprises over 9,500 offices in 79 countries and territories in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa.

HSBC shares are listed on the New York Stock Exchange in the form of American Depositary Receipts, and thus HSBC is subject to the insider lending prohibition of Section 13(k) of the Exchange Act. In addition, HSBC's lead bank subsidiary, HSBC Bank plc, a U.K. bank headquartered in London, maintains a shelf registration and is required to file reports under the Exchange Act (and thus is similarly subject to the insider lending prohibition of Section 13(k)).

Section 13(k) generally prohibits "issuers" from making or arranging for, directly or indirectly, personal loans to their directors and executive officers, subject to certain limited exceptions. Section 13(k) provides a statutory exemption for loans made by U.S. depository institutions whose deposits are insured by the Federal Deposit Insurance Corporation if the loan is subject to the insider lending restrictions of Section 22(h) of the Federal Reserve Act (including the Federal Reserve Board's Regulation O). This statutory exemption is not available to non-U.S. banks, however, and the Proposed Rule is designed to alleviate this disparate treatment.

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While the statutory banking exemption in Section 13(k) permits HSBC's U.S. bank subsidiary, HSBC Bank USA, to make loans to HSBC's directors and executive officers, the statutory banking exemption does not cover insider loans made by HSBC's other bank subsidiaries, including its United Kingdom incorporated bank subsidiary, HSBC Bank plc, and its Hong Kong incorporated bank subsidiary, The Hongkong and Shanghai Banking Corporation Limited ("HSBC Hong Kong"). Thus, unlike a U.S.-based banking organization, HSBC does not have the option of making insider loans from all of its bank subsidiaries under the banking exemption from Section 13(k). HSBC therefore supports the Commission's development of a proposed exemption from Section 13(k) for insider loans by foreign banks. Such an exemption will provide much needed flexibility to foreign banking organizations such as HSBC and will further the U.S. policy of national treatment for foreign banks.

We would, however, offer three suggestions to improve the Proposed Rule, as explained below. First, the Commission should clarify that insider loans that comply in fact with the insider lending restrictions set forth in the Proposed Rule should be exempt from Section 13(k) (i.e., regardless of whether comparable restrictions are embodied in the laws or regulations of the foreign bank's home country). Second, the Commission should revise the board approval requirement to accommodate home country practices that permit board approval to be obtained through a committee of the full board to which authority to approve insider loans is delegated or assigned. Third, the Commission should add to the Proposed Rule specific definitions of the terms "director" and "executive officer" for foreign private issuers, as the Commission did in its Regulation Blackout Trading Restriction ("Regulation BTR") under Section 306(a) of the Sarbanes-Qxley Act.

The Home Country Deposit Insurance or CCS Condition

The first of the three conditions required for an insider loan by a foreign bank to qualify for the exemption in the Proposed Rule would require that the foreign bank that makes the loan be subject to a home country deposit insurance scheme or have obtained a determination by the Federal Reserve Board that the bank is subject to comprehensive consolidated supervision. HSBC supports the Commission's proposal to include these requirements as alternatives. HSBC's lead bank, HSBC Bank plc, is subject to the United Kingdom's mandatory deposit insurance scheme and therefore would qualify for the exemption in Rule 13k-1. In addition, HSBC itself has been the subject of several CCS determinations by the Federal Reserve Board,¹ as has HSBC Hong Kong.² Consequently, under the Proposed Rule, loans by HSBC Bank plc and HSBC Hong Kong to directors and executive officers of HSBC would be exempt from Section 13(k) (provided the other two conditions in the Proposed Rule are satisfied).

¹ See, e.g., HSBC Holdings plc, 81 Fed. Res. Bull. 1037 (1995); HSBC Holdings plc, 83 Fed. Res. Bull. 326 (1997); HSBC Holdings plc, 86 Fed. Res. Bull. 140 (2000).

² See Hongkong and Shanghai Banking Corporation, Ltd., 81 Fed. Res. Bull. 902 (1995).

The Home Country Insider Lending Restriction Condition

The second condition under the Proposed Rule appears to require that a loan to an insider of the bank or the bank's parent company be made in compliance with home country laws or regulations that prohibit insider loans unless they are (1) on market terms; (2) made pursuant to an employee benefit or compensation plan on terms no more beneficial than those offered to the other employees of the foreign bank or its parent; or (3) made following the express approval of the foreign bank's home jurisdiction supervisor. The first two of these requirements are modeled on requirements contained in the Federal Reserve Board's Regulation O.

The Commission's explanation of this "Home Jurisdiction Insider Lending Restriction Condition" at certain places in the Release appears to suggest not only that a loan would need to comply in fact with one of these three requirements, but also that the laws or regulations of the foreign bank's home jurisdiction would need to mandate compliance with the relevant requirement. On the other hand, there are portions of the preamble that are less clear on this point.³

HSBC strongly urges the Commission to clarify its final rule to make clear that an insider loan that complies in fact with one of the three insider lending requirements set forth in the Proposed Rule is exempt from Section 13(k) (assuming the other two conditions in the Proposed Rule are met). Whether compliance with the Proposed Rule's insider lending requirements stems from home country laws or regulations, formal or informal supervisory guidance, private sector banking association standards, or simply the voluntary policies and procedures adopted by the foreign bank's board of directors, we believe that the exemption should be available if the loan satisfies the stated requirements in fact. If a loan by one of HSBC's subsidiary banks to a director of HSBC is made on arm's length terms, it should not matter whether the laws or regulations of the bank's home jurisdiction specifically mandate such terms. The loan itself will have complied with the standards set by the Commission.

To the extent the Commission's exemption for foreign banks looks to the content of a foreign bank's home country laws and regulations, it inevitably will create arbitrary results. Banks in jurisdictions that have elected to embody their insider lending restrictions in laws or regulations will be favored over banks in jurisdictions where insider lending restrictions have been adopted in another form. In addition, the current formulation of the Proposed Rule creates significant potential for uncertainty for banks based in jurisdictions where insider lending restrictions are reflected in supervisory standards whose legal effect may be similar although not identical to laws or regulations.

³ See, e.g., 48 Fed. Reg. 54590,54593 (Sept. 17,2003) ("These conditions would require a foreign bank's loan to an executive officer or director to be either on market terms to unrelated parties or, if pursuant to an employee benefit or compensation plan, on terms no more beneficial to those offered to its other employees. ... Alternatively, a foreign bank insider loan could also qualify for the Section 13(k) exemption if it has received the prior approval of the foreign bank's home jurisdiction supervisor.").

The Board Approval Condition

The third condition in the Proposed Rule would require that the majority of a foreign bank's board of directors approve in advance any loan that, when aggregated with all other loans to a particular director or executive officer, would exceed U.S. \$500,000. The Proposed Rule also would require that the intended loan recipient abstain from voting on the loan. The Release clarifies that if a foreign issuer has a two-tier board structure, where one tier is a supervisory board and the other a management board, majority approval of either board will suffice.

We respectfully suggest that foreign bank issuers should be permitted to meet this board approval requirement with a majority vote of its relevant board or with the approval of a committee of the board to which authority has been delegated or assigned to approve insider loans. In the case of approval by a committee of the board, we believe it would be appropriate to require that the intended recipient of the loan not be a member of the committee.

As the Release acknowledges, the board structures of foreign issuers frequently differ from those in the United States. Home country banking and corporate laws and regulations that require board approval for certain actions such as insider loans may permit committees to approve such actions under delegated authority. In addition, in some jurisdictions committees of the board are permitted to include non-board members and in this regard perform an important corporate governance function. In order to accommodate variations in corporate governance structures and home country banking laws and practices, we believe that it would be appropriate to allow a committee of the board of a foreign bank to approve insider loans (so long as the intended recipient of the loan is not a member of the committee).⁴

Definitions of Directors and Executive Officers

HSBC strongly supports the suggestion made in the comment letter submitted by the Institute of International Bankers that the Commission specifically define the terms "director" and "executive officer" for foreign private issuers for purposes of Section 402 of the Sarbanes-Oxley Act and the Commission's exemption for foreign banks. In adopting Regulation BTR, the Commission determined to adopt such definitions, which were different than the definitions used for domestic issuers, to provide clarity for foreign private issuers in a manner consistent with the purposes of Section 306(a) of the Sarbanes-Oxley Act. In view of the common public policy rationales underlying Sections 306(a) and 402 of the Sarbanes-Oxley Act (the prevention of insider abuse), and a similar need

⁴ In this respect, we would note that the Commission has afforded flexibility to foreign issuers in other rulemakings under the Sarbanes-Oxley Act in recognition of differing corporate governance practices and requirements. See, e.g., SEC Release No. 33-8220 (April 9, 2003) (providing foreign private issuers flexibility in audit committee requirements "to address commenters' concerns regarding the specific areas in which foreign corporate governance arrangements differ significantly from general practices among U.S. corporations").

for clarity in applying the terms “director” and “executive officer” to foreign private issuers, we respectfully suggest that the Commission should adopt the same definitions for purposes of Section 402. That is, the Commission should define the term “director” for foreign private issuers as a director (as defined in Exchange Act Section 3(a)(7)) “who is a management employee of the issuer”⁵ and define the term ““executive officer” for foreign private issuers as “the principal executive officer or officers, the principal financial officer or officers and the principal accounting officer or officers of the issuer.”⁶


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Thank you in advance for considering the issues raised by this comment letter. Please do not hesitate to contact us with any questions or if we can provide any further information.

Yours sincerely



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See Exchange At Rule 100(c)(2).

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See Exchange Act Rule 100(h)(2).