Office of Thrift Supervision
Department of the Treasury

1700 G Street, N.W., Washington, D.C. 20552 • (202) 906-6000

August 11, 1995

MEMORANDUM FOR [redacted]

[redacted] REGION

FROM: Carolyn J. Buck, Chief Counsel

Jeff Miner, Deputy Chief Counsel

Dorene C. Rosenthal, Senior Attorney

SUBJECT: Authority of Federal Savings Associations To Offer Foreign Currency Exchange Services

I. Introduction and Summary of Conclusions

This responds to your inquiry regarding whether federal savings associations may offer foreign currency exchange services to their customers.

For reasons explained more fully below, we conclude that federal savings associations may offer foreign currency exchange services pursuant to the incidental powers doctrine, provided such services are offered in a manner consistent with safety and soundness. Federal savings associations are not authorized to speculate in foreign currency. Accordingly, federal savings associations may invest in and hold foreign currency only to the extent: (a) necessary to facilitate their currency exchange services, and (b) consistent with safety and soundness.

II. Background

You have advised us that a federal savings association in the [redacted] Region, [redacted] (the "Association"), is currently providing foreign currency services to its customers. The Association is controlled by [redacted] (the "Holding Company"), a [redacted] financial corporation. The Association's exchange program serves primarily the retail customers of the Association, approximately ninety percent of whom are [redacted] who reside in [redacted] for part of the year, as well as other [redacted] visitors to the area. Local merchants also utilize the Association's currency exchange services.

The currency exchanges executed by the Association as principal involve the purchase and sale of [redacted] Dollars in exchange for U.S. Dollars up to a maximum amount of $[redacted] ([redacted]) per transaction. The Association estimates that ninety-five percent of customer transactions under the program are in amounts of less than $[redacted] ([redacted]). For transactions under $[redacted] ([redacted]), the Association sets buy/sell rates of exchange each day and customer service representatives execute the transactions. Transactions in amounts between $[redacted] and $[redacted] ([redacted]) are handled by an officer of the Association.

On some occasions, the Association is requested to exchange currency other than [redacted] Dollars or to exchange more than $[redacted] ([redacted]) in a single transaction. In these instances, the Association acts on an agency basis on behalf of its Holding Company, which establishes the exchange rate and assumes the risk of currency fluctuations.

The Association takes no positions in [redacted] Dollars or any other foreign currency for speculative purposes. At the height of the season when [redacted] are living in or visiting [redacted] the Association keeps a maximum of $[redacted] ([redacted]), which equates to approximately $[redacted] (U.S.), in its vault overnight to accommodate customer demand.

III. Discussion

Although federal savings associations have previously been authorized to provide foreign currency exchange services indirectly through their service corporation subsidiaries,[1] neither the Office of Thrift Supervision ("OTS") nor its predecessor, the Federal Home Loan Bank Board, has ever addressed whether federal savings associations may offer foreign currency exchange services directly.

While there is no provision in the Home Owners' Loan Act ("HOLA") that expressly authorizes federal savings associations to exchange foreign currency, we believe this activity is permissible pursuant to the incidental powers doctrine. Last year, the OTS issued an opinion that provides a comprehensive overview of the relevant case law regarding incidental powers and draws from it a four-part test for identifying activities that fall within the incidental powers of federal savings associations.[2] Our analysis below is based on this four-part test.

A. Is the activity consistent with the purpose and function Congress envisioned for federal savings associations, as manifest in the legislative history of the HOLA?

As is explained in detail in the above-referenced opinion, Congress has made various amendments to the HOLA over the past two decades that, inter alia, have expanded and modernized the role of federal savings associations, while strengthening the safety and soundness framework within which they operate. The legislative history of these amendments indicates that Congress intended to give federal savings associations "flexibility . . . to improve the range of services . . . [provided] to their customers,"[3] and to "enhance the ability of thrifts to offer complete financial services

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[1] FHLBB Res. No.72-252 (Feb. 29, 1972).

[2] See OTS Op. Chief Counsel (Mar. 25, 1994) (concluding under four-part test that federal savings associations can provide certain basic postal services in their retail offices).

[3] H. Conf. Rep. No. 899, 97th Cong., 2d Sess. 87 (1982).

to the consumer."[4] Congress' objective was to enable federal savings associations to meet the needs of ordinary consumers "across the board" in "one-stop family financial centers."[5] In addition, over the past two decades, Congress has also authorized savings associations to expand into commercial banking on a small scale.[6]

Currency exchange is a basic financial service required by, inter alia, tourists and business travelers, seasonal residents, persons living near international borders, and many retail businesses, especially when located in areas with significant concentrations of tourists, travelers, and seasonal residents. Substantial convenience and efficiency is achieved by permitting these persons and businesses to exchange foreign currency and conduct their other financial business in "one-stop" at a single "financial center," rather than requiring them to obtain financial services from multiple providers. Allowing savings associations to provide foreign currency exchange services would, thus, be consistent with the role Congress envisioned for savings associations as full-service financial centers.

B. Does the activity facilitate the conduct of an activity expressly authorized by Congress for federal savings associations?

Another test that the courts often employ when considering whether an activity falls within the incidental powers of a financial institution is whether the activity facilitates the conduct of one of the institution's express powers.

Foreign currency exchange services facilitate one of the core businesses of savings associations -- deposit taking. For example, in the present instance, the Association represents that a substantial percentage of the customers utilizing its foreign currency exchange services have deposit accounts at the Association. Upon arriving in the U.S. from [redacted] seasonal residents of the Association routinely hold

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[4] S. Rep. No. 368, 96th Cong., 1st Sess. 13 (1979).

[5] Id.

[6] See e.g., 12 U.S.C.A. § 1464(c)(2)(A) and (D) (West Supp. 1995) (authorizing investments in commercial loans and corporate debt securities).

[redacted] currency that they wish to deposit into their accounts. Upon departing, seasonal residents routinely wish to withdraw funds from their accounts in the form of [redacted] currency. Similarly, merchants and residents located in areas with many seasonal residents or tourists or near an international border also frequently receive foreign currency that they wish to deposit, or need to make withdrawals in foreign currency to facilitate their dealings with foreigners. Thus, foreign currency exchange is often an essential aspect of providing effective depository services.

Foreign currency exchange is also closely tied to two other well-established activities of savings associations -- selling and redeeming travelers checks[7] and issuing credit cards.[8] Customers who need travelers checks frequently also need foreign currency and vice versa. Foreign currency exchange is, thus, an important component part of meeting the basic financial needs of customers preparing to travel. Someone preparing to travel abroad is unlikely to elect to purchase travelers checks at one location and exchange foreign currency at another. It is questionable whether savings associations can provide meaningful travel-related financial services if they are unable to exchange foreign currency.

Similarly, travelers have become accustomed to being able to use their credit cards abroad. Foreign merchants frequently honor credit cards issued by U.S. creditors. These merchants debit the customer's credit card in the currency of the country where the purchase is made and expect to be paid by the credit card issuer in that currency. Charges incurred in a foreign country must nevertheless be converted to U.S. dollars for purposes of billing the credit card holder. Thus, foreign currency exchange is also an integral part of providing effective credit card services.

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[7] FHLBB Op. Gen. Counsel (Nov. 24, 1965); FHLBB Op. by Williams (Mar. 16, 1988). See also Arnold Tours v. Camp, 472 F.2d 427 (1st Cir. 1972).

[8] 12 U.S.C.A. § 1464(b)(4) (West Supp. 1995).

C. Does the activity relate to the financial intermediary role that all federal savings associations were intended to play?

Another test commonly employed to determine whether an activity is properly incident to the business of a financial institution is the financial intermediary test. The courts have recognized that, when reduced to their essence, financial institutions serve as financial intermediaries, facilitating the flow of money and credit among different parts of the economy. As the Supreme Court has noted, "[t]he very object of banking is to aid the operation of the laws of commerce by serving as a channel for carrying money from place to place. . . ."[9]

Exchanging foreign currency for U.S. dollars, and vice versa, is critical to the unimpaired flow of commerce, especially in areas of the country like [redacted] that attract large numbers of foreign tourists and seasonal residents. Currency exchange permits foreign customers to easily engage in commerce in the U.S. and U.S. customers to easily engage in commerce abroad. Thus, exchanging foreign currency is a basic part of financial intermediation.

D. Is the activity necessary to enable federal savings associations to remain competitive and relevant in the modern economy, thereby permitting federal savings associations to fulfill the purposes for which they were created?

When assessing whether an activity falls within the scope of a financial institution's incidental powers, the courts also frequently consider whether institutions of the type in question need to engage in the activity in order to keep pace with changes in the modern economy. When employing this test, the courts often consider whether the activity is one that customers have come to expect financial institutions to perform as a matter of convenience and/or whether financial institutions need to engage in the activity in order to keep pace with their competitors.

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[9] Auten v. United States National Bank, 174 U.S. 125, 143 (1899).

National banks and many state banks are permitted to exchange foreign currency for customers.[10] As a result, many customers have become accustomed to the convenience of exchanging foreign currency at depository institutions. As is pointed out in the discussion above, it is unlikely that customers who have frequent foreign exchange needs (e.g., frequent travellers, seasonal residents, persons living near international borders, and retail businesses located in these areas) will elect to conduct their banking business at savings associations if savings associations cannot exchange foreign currency. Moreover, as the modern economy becomes increasingly international, the importance of currency exchange is growing.

Based on the foregoing, we conclude that each of the factors commonly considered by the courts to determine whether an activity falls within the scope of an institution's incidental powers supports the conclusion that federal savings associations may offer foreign currency exchange services to their customers. Accordingly, federal savings associations may engage in this activity, provided they do so in a safe and sound manner.

We have consulted with Supervision Policy regarding the Association's foreign currency exchange program. Because the Association has structured its program so as to avoid significant currency risk, Supervision Policy has advised us that it has no objection to the Association's program. Accordingly, provided the [redacted] Region has no safety and soundness concerns, the Association may continue its foreign exchange program.

In reaching the foregoing conclusions, we have relied on the factual representations made in the materials you provided and in the supplemental materials submitted by the Association, all as summarized herein. Our conclusions depend on the accuracy and completeness of those facts. Any material differences in facts or circumstances from those described herein could result in different conclusions.

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[10] See 12 U.S.C.A. § 24 (West 1989); and FFIEC Joint Notice of Uniform Guidelines on Internal Control for Foreign Exchange Activities in Commercial Banks (effective June 11, 1980).

If you have further questions, please feel free to contact Dorene Rosenthal, Senior Attorney, at (202) 906-7268.

cc: Regional Directors
Regional Counsel

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