

CHAPTER 6**Regulation and Supervision of Banks****SECTIONS**

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§ 601. Regulation and supervision of banks—General policies.

(1) All domestic banks and, to the extent of and with respect to business done at any branches established in the Federated States of Micronesia, all foreign banks doing business in the Federated States of Micronesia shall be regulated and supervised by the Banking Board in such manner as to secure the safe and sound conduct of such business, to prevent unsound practices, and to maintain the public confidence in such business and protect the public interest and the interests of depositors.

(2) In determining if a Bank is carrying on its business in a prudent manner, the Banking Board will have regard to the following:

(a) capital adequacy in relation to the size and nature of the business;

(b) asset concentration and risk exposure;

(c) separation of Banking Business from other business and from other interests of any person owning or controlling the Bank;

(d) adequacy of liquidity in relation to liabilities;

(e) asset quality and adequacy of provisions for losses;

(f) internal controls, risk management and accounting systems;

(g) adequacy of governance arrangements (including Directors and senior management) in relation to the nature and scale of the business; and

(h) such other matters as the Banking Board considers relevant.

(3) Every foreign bank licensed pursuant to section 501 of this subtitle shall, with the concurrence of the Banking Commissioner, designate the branch in the Federated States of Micronesia which may be used as the channel of communication between the Banking Board and the Bank with respect to the application of this subtitle to its business throughout the Federated States of Micronesia. Such branch shall be responsible for the timely provision of reports and information by other branches requested under this subtitle. The head office of a domestic bank shall be the channel of communication between the Banking Board and its branches, and shall be responsible for the timely provision of reports and information by other branches requested under this subtitle.

(4) All FDBs shall comply with all existing and future banking and banking-related laws, rules and regulations of the United States relating to supervision, regulatory, and resolution and receivership matters, except any portions of such laws, rules and regulations that conflict with sections 4 or 5 of Article XIII of the FSM Constitution.

Source: PL 1-94 § 601(1); PL 9-130 § 24; PL 12-57 § 10; PL 13-56 § 4.

Case annotations: Questions regarding the validity of the provisions of promissory notes for personal loans, executed with a national

bank operating in each state of the FSM and having in part foreign ownership, are closely connected to the powers of the national legislature to regulate banking, foreign and interstate commerce, and bankruptcy, and to establish usury limits, and they have a distinctly national character. The FSM Supreme Court therefore will formulate and apply rules of national law in assessing such issues. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 218 (Pon. 1990).

The FSM Supreme Court will consider an unambiguous provision in a promissory note for the payment of reasonable attorney's fees in debt collection cases as valid in the FSM. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 219 (Pon. 1990).

Because agreements in promissory notes for the payment of attorney's fees are essentially indemnity clauses, they will be given effect only to the extent that expenses and losses are actually incurred, as demonstrated by detailed supporting documentation showing the date, the work done, and the amount of time spent on each service for which a claim for compensation is made. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 219 (Pon. 1990).

Provisions in promissory notes for the payment of attorney's fees will be enforced only to the extent that the fees demanded are reasonable. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 219 (Pon. 1990).

Where attorney's fees claimed pursuant to a contractual provision are excessive or otherwise unreasonable, it is within the equitable and discretionary power of the court to reduce or even deny the award, despite the contractual provision. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 220 (Pon. 1990).

Except in unusual circumstances, the amount awarded pursuant to a stipulation for the payment of attorney's fees in debt collection cases in the FSM will be limited to a reasonable amount not in excess of fifteen percent of the outstanding principal and interest. *Bank of Hawaii v. Jack*, 4 FSM R. 216, 221 (Pon. 1990).

§ 602. Regulations—Issuance and promulgation.

(1) For the purpose of effectuating the policy declared in section 601 of this chapter, the Banking Board, with the approval of the President of the Federated States of Micronesia, may adopt regulations consistent with law and sound banking practice.

(2) Such regulations shall be brought to the attention of those affected thereby in the manner that the Banking Board may prescribe.

Source: PL 1-94 § 601(2).

Cross-reference: The statutory provisions on the President and the Executive are found in title 2 of this code. The statutory provisions on Administrative Procedure are found in title 17 of this code.

§ 603. Examination of banks—Authority; Testimony; Document Production; Fees.

(1) The Banking Commissioner may examine, or cause to be examined, every domestic or foreign bank for the purpose of ascertaining whether it has complied with this subtitle and other applicable laws and for such other purposes and such other matters as the Banking Board may prescribe.

(2) The Banking Commissioner and every examiner appointed by him may administer an oath to any person whose testimony may be required on the examination of any bank and summon and compel the appearance and attendance of any person for the purpose of the examination.

(3) As part of any examination, the Banking Commissioner may also require the production of books, records or other documents in whatever form.

(4) As an examination fee, each bank so examined shall pay the total cost of such examination, and the sum so paid shall be deposited into the General Fund of the Federated States of Micronesia.

Source: PL 1-94 § 602; PL 2-20 § 8; PL 9-130 § 25; PL 13-56 § 5.

Editor's note: Subsections (1) and (2) were originally a single subsection.

§ 604. Report of banks.

(1) Every domestic or foreign bank shall make at least one report of its condition each year to the Banking Commissioner within 90 days after the close of the bank's fiscal year, and according to forms to be prescribed by him, verified by the oath of the chief executive officer or chief financial officer and attesting officer, certifying and subscribing under oath that each of them has personal knowledge of the facts stated therein and that the same are true.

(2) Such reports shall exhibit in detail and under appropriate heads the total resources and liabilities of the bank, and, in the case of a foreign bank, shall show separately the resources, liabilities, and operations in the Federated States of Micronesia.

(3) The Banking Commissioner shall have the right to require that any such reports be audited at the bank's expense by independent accountants approved by the Banking Commissioner.

(4) Every domestic and foreign bank holding a license under this subtitle shall forward to the Banking Commissioner no later than the 31st day of December each year a report outlining the bank's policy regarding employment of citizens of the Federated States of Micronesia in executive positions in the bank, and the steps being taken to maximize such employment.

(5) Every domestic and foreign bank shall publish in such manner as the Banking Commissioner shall direct, within four months after the close of its fiscal year, an audited report of its condition as described in subsections (1) and (2) of this section.

(6) Each Bank shall deliver to the Banking Board within such period as may be specified and in such form as the Board may from time to time approve, a periodic statement of its:

- (a) assets and liabilities;
- (b) earnings and expenses;

- (c) loans and advances; and
- (d) such other data as the Board may deem necessary to carry out the purpose of this Act.

Source: PL 1-94 § 603(1); PL 2-20 § 9(part); PL 9-130 § 26; PL 12-57 § 11.

§ 605. Special reports.

- (1) The Banking Commissioner may request from the banks special reports.
- (2) The Banking Commissioner may, from time to time, by notice in writing, require any domestic or foreign bank to submit such reports and returns as he may require for the purposes of the administration and enforcement of the provisions of this subtitle and any regulations made thereunder.
- (3) Any bank notified in writing under subsection (2) of this section shall comply with accurate and timely submissions or be subject to a penalty imposed by the Banking Board in an amount not to exceed \$100 per day until the correct information has been provided to the satisfaction of the Banking Commissioner.
- (4) During the first five years of operations in the Federated States of Micronesia by any domestic bank, the Banking Commissioner shall call for special reports of its condition not less frequently than each calendar quarter.

Source: PL 1-94 § 603(2); PL 2-20 § 9 (part); PL 9-130 § 27; PL 12-57 § 12; PL 13-56 § 6.

§ 606. Misleading or obstructive conduct an offense.

- (1) Whoever, with intent to deceive:
 - (a) makes a false or misleading entry in any bank book or record;
 - (b) makes, provides or certifies any report required by section 604 or 605 of this subtitle, or provides any information required under this subtitle, which is false in any material particular;
 - (c) omits an entry or alters or conceals any entry in any bank book or record; or
 - (d) conceals or destroys any information, book, voucher, record, report, return, minutes or document relating to the accounts, transactions, affairs or business of a bank;

shall be fined not more than \$1,000, or imprisoned for not more than one year, or both.

- (2) Whoever obstructs, or endeavors to obstruct:
 - (a) the proper performance by an Auditor of a Bank of his duties related to that Bank;
 - (b) an examination of a Bank conducted pursuant to section 603 of this subtitle; or
 - (c) the proper performance of his duties by an advisor appointed under section 701 of this subtitle;

shall be fined not more than \$1,000, or imprisoned for not more than one year, or both.

Source: PL 1-94 § 603(3); PL 2-20 § 9 (part); PL 12-57 § 13.

§ 607. Penalty for failure to report.

Any bank which fails to make, transmit, and publish any report required under sections 604 or 605 of this chapter shall be subject to a fine of \$100 per day for each day's delay after the period specified in this section.

Source: PL 1-94 § 603(4); PL 2-20 § 9 (part).

§ 608. Alternative examination and reports.

(1) The Banking Commissioner may accept, in lieu of the examination required or authorized by section 603 of this chapter, the most current examination made by the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, or a Federal Reserve Bank, or in case of a foreign bank not examined by such agencies, an examination acceptable by the appropriate government agency in the home jurisdiction of that bank.

(2) The Banking Commissioner may accept, in lieu of any report of condition which may be required by sections 604 or 605 of this chapter, a report of condition obtained by said Corporation, Board of Governors, Federal Reserve Bank, or government agency.

Source: PL 1-94 § 604; PL 2-20 § 10; PL 9-130 § 28.

§ 609. Legal reserve—Domestic banks.

(1) Subject to such additional requirements as the Banking Board may impose, every domestic bank shall maintain a legal reserve which shall not be less than 20 percent of its demand deposits and not less than five percent of its other deposits. Said reserve shall consist of United States currency or demand deposits in the name of such bank deposited in another bank approved for such purpose by the Banking Board.

(2) The Banking Board may increase or decrease the minimum legal reserve for demand deposits established in this section up to not more than 30 percent or down to not less than 15 percent of the total demand deposits of a domestic bank, when in its judgment the circumstances so require it; but the order increasing or decreasing the minimum legal reserve shall not be effective until 30 days after it is entered. This time might be extended by the Banking Board.

Source: PL 1-94 § 605(1); PL 2-20 § 11 (part).

§ 610. Legal reserve—Foreign banks.

Every foreign bank shall maintain, with respect to its deposits in the Federated States of Micronesia, a legal

reserve which shall not be less than, and which shall be subject to the same condition as, the legal reserve requirement imposed in the jurisdiction of its place of incorporation on deposits of the foreign bank in that jurisdiction.

Source: PL 1-94 § 605(2); PL 2-20 § 11 (part).

§ 611. Legal reserve—Notification.

The Banking Commissioner shall notify any domestic or foreign bank whose legal reserve is less than that required by this subtitle of its obligations to make up the full amount. If such bank fails to do so within a period of 30 days, it may be declared in liquidation by the Banking Board. In such event, the Banking Commissioner shall apply to the Trial Division of the Supreme Court of the Federated States of Micronesia for the appointment of a receiver to take charge of and wind up the affairs of such bank and thereafter the matter shall be governed by the provisions of section 802 of this subtitle.

Source: PL 1-94 § 605(3); PL 2-20 § 11(part); PL 9-130 § 29.

Cross-reference: The statutory provisions on the FSM Supreme Court are found in title 4 of this code.

The FSM Supreme Court website contains court decisions, rules, calendar, and other information of the court, the Constitution, the code of the Federated States of Micronesia, and other legal resource information at <http://www.fsmsupremecourt.org/>.

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612. Limitations on loans—Maximum amount.

(1) No domestic bank shall permit a person to become indebted or liable to it, either directly or indirectly, in an amount in excess of 20 percent of the aggregate paid-in and unimpaired capital, surplus, and undivided profits of the bank; PROVIDED however, that this subsection shall not apply to transactions entered into with another bank which is a member of the Federal Deposit Insurance Corporation of the United States, and for which quarterly reports of condition are monitored.

(2) In computing the total liabilities, direct or indirect, of any person to a bank, there shall be included all liabilities to the bank of any related person and any loans made for his benefit or for the benefit of any related person.

(3) In computing the total liabilities of any firm, copartnership, or unincorporated association to the bank, there shall be included all liabilities of its individual members and all loans made for the benefit of the copartnership or unincorporated association or any members thereof.

(4) In computing the total liabilities of any corporation to a bank there shall be included all liabilities of and all loans made for the benefit of the corporation and its majority owned subsidiaries.

Source: PL 1-94 § 606(1); PL 12-57 § 14.

§ 613. Limitations on loans—Related persons.

(1) Except as herein provided, no domestic bank shall make any extension of credit to any of its officers, directors, agents, or employees, or to any related person, either directly or indirectly, except upon the written application of such person or related person stating the line of credit applied for, terms and security, if any, offered therefore to the board of directors or to the loan or executive committee of the board, and then only with the written approval of a majority of the board or majority of the loan committee of the bank (excluding the person seeking the credit) before the loan is made; and the approval of the loan as allowed by the board or the loan committee of the bank shall be made part of the minutes of the next directors' meeting of the bank.

(2) Loans may be made to any officer, director, agent, employee, or shareholder of any domestic bank or any related person, without such application and approval, in amounts not in excess of \$25,000 in aggregate principal owing by any such individual and related person at any one time.

Source: PL 1-94 § 606(2); PL 12-57 § 15; PL 13-56 § 7; PL 16-16 § 1.

§ 614. Limitations on loans—Use of bank's security; Purchase of bank's stock.

No domestic bank shall make any loan on the security of its own stock or for the purchase of its own stock.

Source: PL 1-94 § 606(3).

§ 615. Limitations on loans—Liability for violations.

Any officer, director, agent, or employee of any bank who knowingly permits the funds of the bank to be loaned in a dishonest manner or contrary to sections 612, 613, or 614 of this chapter shall be held responsible in his individual capacity for all damages which the bank, its shareholders, depositors, creditors, or any persons shall have sustained in consequence thereof.

Source: PL 1-94 § 606(4).

§ 616. Prohibited loans and withdrawals—Penalties.

Any director, officer, or employee of a bank or related person who asks for or receives any commission, money, property, or thing of value for his own personal benefit for procuring or assisting in procuring a loan from such bank or for permitting any person to overdraw any account with such bank shall be fined not more than \$1,000, or imprisoned not more than one year, or both.

Source: PL 1-94 § 607(1).

§ 617. Applications for credit—Denials and records.

Each bank must provide an applicant with a written explanation of the basis on which a decision is made to deny a written application for a loan, a credit card, or other request for extension of credit within 30 days from the date of receipt of such application by the bank. Each bank shall keep records of all applications for credit received and denials and written explanations given in the manner determined by the Banking Commissioner.

Source: PL 6-41 § 3; PL 13-56 § 8.

Editor's note: The word "Denials" in the section title was not capitalized in PL 13-56 § 8, but was capitalized here for format consistency.

§ 618. Prohibited investments by domestic banks.

No domestic bank shall invest in the stock of any other corporation, acquire any real estate, except with the approval of the Banking Board for use as its principal office in the Federated States of Micronesia, or pledge any of its assets as security for or guaranty any obligations of others except for the issuance of its letters of credit in connection with the shipment of goods.

Source: PL 1-94 § 607(2); renumbered by PL 6-41 § 4.

§ 619. Acceptance of deposits—Minimum capital requirements.

No domestic bank may accept deposits at any time that its paid-in capital, surplus, and undivided profits is less than \$1,000,000 in the aggregate.

Source: PL 1-94 § 607(3); renumbered by PL 6-41 § 4; PL 13-56 § 9.

§ 620. Declarations of dividends—Requisites.

No domestic bank shall declare any dividend or make any other distribution to its stockholders except:

- (1) out of earnings for the current and next preceding year; or
- (2) with the approval of the Banking Board.

Source: PL 1-94 § 607(4); renumbered by PL 6-41 § 4.

§ 621. Bank stock—Ownership limitations.

No person or group of related persons (including entities that are affiliated as parent or subsidiary companies or are otherwise under common control) may acquire ten percent or more of the stock of a domestic bank without the prior approval of the Banking Board.

Source: PL 1-94 § 607(5); renumbered by PL 6-41 § 4; PL 13-56 § 10.

§ 622. Limitations on sale of assets, merger, etc.

No domestic bank may merge or consolidate with, or sell a substantial portion of its assets to, another bank without the approval of the Banking Board. No foreign bank may make any arrangement or enter into any agreement for the sale or disposal of its business, or part thereof, in the Federated States of Micronesia to any other person without the prior approval in writing of the Banking Board.

Source: PL 1-94 § 607(6); renumbered by PL 6-41 § 4; PL 12-57 § 16.

§ 623. Deposit and other insurance.

(1) If and while it is available under the laws of the United States, all domestic banks and foreign banks, as a condition to operating an office or branch in the Federated States of Micronesia, shall secure their depositors by deposit insurance of the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation of the United States, or their successor entities.

(2) All domestic and foreign banks operating an office or branch in the Federated States of Micronesia shall provide themselves with protection and indemnity against burglary, embezzlement, and other similar insurable loss. If a domestic or foreign bank refuses to comply with this requirement, the Banking Commissioner shall have the right to make arrangements to furnish such protection and indemnity, charging the cost thereof to said bank.

Source: PL 1-94 § 608; PL 2-20 § 12; renumbered by PL 6-41 § 4; PL 9-130 § 30.

§ 624. Prohibited interests of Government officials in banks; Removal from office.

(1) No member of the Banking Board nor the Public Auditor nor any representative of the Banking Board or the Public Auditor nor any bank examiner shall, during the discharge of his office:

- (a) be an officer, director, or employee in any bank or company affiliated therewith;
- (b) own or deal directly or indirectly in the shares or obligations of such bank or affiliated company;
- (c) be interested in or receive directly or indirectly from such bank or affiliated company, or from any of its officers, directors, or employees, any salary, gratuity, compensation, or other thing of value by way of gift, credit, compensation for services, or for any other reason; or

(d) be interested in or under obligation to negotiate any loan, obligation, or settlement for another person with such bank or affiliated company.

(2) Any violation of this section by any official or employee referred to herein shall be sufficient cause for his removal from office by the President.

Source: PL 1-94 § 609(1); renumbered by PL 6-41 § 4.

Cross-reference: The statutory provisions on the President and the Executive are found in title 2 of this code. The statutory provisions on the Public Auditor are found in chapter 5 of title 55 (Government Finance and Contracts) of this code.

§ 625. Permissible interests of Government officials.

Notwithstanding the provisions of section 624 of this chapter, any official or employee referred to in such section may own or keep one or more bank accounts, either commercial or savings, and may rent safe-deposit boxes in any bank referred to in such section and doing business in the Federated States of Micronesia, and may obtain a loan from any such bank, foreign bank, or affiliated company; provided, that such official or employee makes full disclosure thereof to the Banking Board and, in the case of each of the members of the Banking Board, he shall make the disclosure to the President of the Federated States of Micronesia.

Source: PL 1-94 § 609(2); renumbered by PL 6-41 § 4.

Cross-reference: The statutory provisions on the President and the Executive are found in title 2 of this code.

§ 626. Filing fees; Disposition of fines.

(1) Every domestic bank or foreign bank in the Federated States of Micronesia shall, upon filing its articles of incorporation in the Office of the Registrar of Corporations, pay a filing fee of \$50.

(2) Every domestic or foreign bank desiring to file in the Office of the Registrar of Corporations articles amendatory or supplementary or a certificate of increase or decrease of capital stock shall pay a fee of \$25.

(3) The fee for furnishing a certified copy of any of the documents referred to in the preceding subsections of this section shall be fifty cents per folio, but not less than five dollars.

(4) All fees required under the provisions of this subtitle shall be paid to the Office of the Registrar of Corporations and shall be accounted for and deposited into the General Fund of the Federated States of Micronesia.

(5) All fines under this subtitle shall be paid to the Banking Commissioner and shall be accounted for and deposited into the General Fund of the Federated States of Micronesia.

Source: PL 1-94 § 610; PL 2-20 § 13; renumbered by PL 6-41 § 4; PL 9-130 § 31.

Cross-reference: The statutory provisions on Corporations and Business Associations are found in title 36 of this code.

§ 627. General penalties.

(1) For any violation of this subtitle, license conditions imposed by the Banking Board pursuant to section 501 of this subtitle, directives issued by the Banking Board pursuant to section 701 of this subtitle, or the regulations prescribed pursuant to section 602 of this chapter, the delinquent domestic or foreign bank shall be subject to a fine of not more than \$5,000 and if the violation is a continuing one, to a further fine not exceeding \$1,000 for every day during which the violation continues; and, in the case of a material violation, to the cancellation of its license.

(2) The Banking Board must give notice to the Bank concerned of the intention to impose a penalty pursuant to subsection (1) of this section, and allow it a hearing in respect to the alleged violation. The Banking Board must take into account the outcome of the hearing in its final decision.

(3) The Banking Commissioner shall immediately notify the Bank concerned in writing of any penalty imposed pursuant to subsections (1) and (2) of this section. If the penalty involves cancellation of license, the Bank must immediately cease to carry on banking business, the Banking Commissioner must notify the Registrar of Corporations of the cancellation, and the provisions of section 801 of this subtitle shall apply.

Source: PL 1-94 Ch. 7; PL 2-20 § 14; renumbered by PL 6-41 § 4; PL 9-130 § 32; PL 12-57 § 17.

Cross-reference: The statutory provisions on Corporations and Business Associations are found in title 36 of this code.