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Regulation of Foreign Banks Operating in the United States: A State Regulator's Controversial Pursuit of a London-Based Bank

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Cover Page Footnote

J.D. Candidate, Fordham University School of Law, 2014; B.A., University of Michigan, 2010. I would like to thank my family and friends for their encouragement throughout my entire lifetime. I would also like to thank my advisor, Professor Sean Griffith, for his guidance and recommendations regarding this subject matter. Finally, I would like to thank my father who, although no longer with us, showed me how to be strong and courageous in the face of adversity.

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ABSTRACT

Benjamin M. Lawsky and the New York State Department of Financial Services upended the regulatory dynamics of the international banking world in August of 2012 when the New York agency reached a staggering settlement with Standard Chartered Bank. The Department of Financial Services accused the bank, which is headquartered in London, but maintains a profitable branch in New York, of violating laws related to United States sanctions imposed upon certain financial transactions with Iran. Although allegations of this sort are not unprecedented, Lawsky's actions and the $340 million settlement were alarming because, in this case, the state regulator acted without any involvement from federal regulators, who were "on the verge of concluding" that the majority of Standard Chartered's transactions with Iran were legal.

The settlement illustrates the tension between state and federal regulators when confronted with alleged violations of law committed by a foreign bank. Specifically, the settlement raises the question of whether a state regulator should be involved in the regulation of a foreign bank operating in the United States, particularly when the bank is primarily violating federal laws that implicate issues of foreign policy. This Comment examines these issues, starting with an introduction of the statutory framework regarding the regulation of foreign banks, followed by a discussion of the various reactions to the Standard Chartered settlement, both positive and negative. This Comment then provides recommendations for resolving the issues raised by the settlement, ultimately concluding that the principle of

* J.D. Candidate, Fordham University School of Law, 2014; B.A., University of Michigan, 2010. I would like to thank my family and friends for their encouragement throughout my entire lifetime. I would also like to thank my advisor, Professor Sean Griffith, for his guidance and recommendations regarding this subject matter. Finally, I would like to thank my father who, although no longer with us, showed me how to be strong and courageous in the face of adversity.

comity paves the way for proper coordination and deference to the appropriate authority—whether state or federal—in the case of overlapping regulatory jurisdiction.

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INTRODUCTION

On August 6, 2012, the New York State Department of Financial Services ("DFS") issued an order pursuant to New York Banking Law Section 39, accusing Standard Chartered Bank ("Standard Chartered") of engaging in illicit dollar-clearing transactions with Iran.[1] The order directed Standard Chartered, a London-based bank, to appear and explain apparent violations of law; demonstrate why Standard Chartered's license to operate in the State of New York should not be revoked; demonstrate why Standard Chartered's United States dollar clearing operations should not be suspended pending a formal license revocation hearing, and submit to and pay for an independent, on-premises monitor of the DFS's choosing to ensure compliance with rules governing the international transfer of funds.[2] On August 14, 2012, one day before Standard Chartered was to appear before the DFS, the parties agreed to settle the matters in the DFS order from August 6, 2012.[3] The settlement required Standard Chartered to pay a civil penalty of $340 million to the DFS.[4] Notably, the order and the ensuing settlement took place without any intervention from or coordination with federal regulators.[5]

While some commentators lauded the DFS and its superintendent Benjamin M. Lawsky for their aggressive stance against violations of federal and state banking laws, others criticized the settlement as a rogue undertaking that failed to allow federal regulators an adequate opportunity to intervene in the matter.[6] Whether Mr. Lawsky and the

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1. *See* Order Pursuant to N.Y. Banking Law § 39, Standard Chartered Bank, 1 (NYS Dep't. of Fin. Servs. Aug. 6, 2012), http://www.dfs.ny.gov/about/ea/ea120806.pdf.

2. *Id.* at 2.

3. *See* Press Release, Dep't of Fin. Servs., Statement from Benjamin M. Lawsky, Superintendent of Financial Services, Regarding Standard Chartered Bank (Aug. 14, 2012), *available at* http://www.dfs.ny.gov/about/press/pr1208141.htm.

4. *Id.*

5. *See* Jessica Silver-Greenberg, *Laundering Case Settled by Bank for $340 Million*, N.Y. TIMES, Aug. 15, 2012, at A1, *available at* http://www.nytimes.com/2012/08/15/business/standard-chartered-settles-with-new-york-for-340-million.html?pagewanted=all.

6. *Compare* Jonathan Weil, *Standard Chartered Fought the Lawsky and the Lawsky Won*, BLOOMBERG (Aug. 16, 2012, 6:30 PM), http://www.bloomberg.com/news/2012-08-16/standard-chartered-fought-the-lawsky-and-the-lawsky-won.html (explaining that the public benefits from having an active, competent, and functional state regulator that is willing to seek large penalties from banks), *with* Peter J. Henning, *What's Next in the Standard Chartered Case*, DEALBOOK (Aug. 8, 2012, 4:43 PM), http://dealbook.nytimes.com/2012/08/08/whats-next-in-the-standard-chartered-case/ (discussing the problems that arose due to the lack of coordination between the DFS and federal regulators), *and* Somasekhar Sundaresan, *New York State Erodes Rule of Law with Standard Chartered Bank*, BUSINESS STANDARD (Aug. 20, 2012), http://www.business-standard.com/india/news/new-york-state-erodes-rulelawstandard-

DFS deserve praise or criticism, the settlement between the DFS and Standard Chartered raises some serious regulatory issues regarding the extent to which a state regulator should be involved in the regulation of a foreign bank operating in the United States, particularly when the bank is primarily violating federal laws that implicate issues of foreign policy.[7]

Part I of this Comment will describe the role of foreign banks in the United States banking system and the statutory framework regarding the regulation of those banks. Part II will parse out the issues arising from the DFS settlement with Standard Chartered and will discuss the positive and negative responses to the settlement. Finally, Part III of this Comment will address the framework required to alleviate the issues arising from overlapping regulatory jurisdiction, concluding that the basic principle of comity paves the way for proper coordination and deference to the appropriate regulatory authority.

I. FOREIGN BANKS OPERATING IN THE UNITED STATES

Part I of this Comment provides a background of foreign banking operations in the United States and the statutory framework regarding the regulation of those banks. Specifically, this Part describes the federal regulatory scheme that Congress has implemented through the International Banking Act of 1978 ("IBA") and the Foreign Bank Supervision Enhancement Act of 1991 ("FBSEA"). It then discusses the remaining power of state regulators over foreign banks, including an explanation of the DFS's powers, such as the ability to utilize Section 39 of the New York Banking Law.

A. RISE IN FOREIGN BANKING OPERATIONS IN THE UNITED STATES

Foreign banks are permitted to operate in the United States through various corporate forms.[8] The decision regarding how to enter and

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chartered-bank/483734/ (suggesting that it is improper for a state regulator to involve itself in issues relating to international relations between the United States and a foreign nation).

7. *See generally* Janet Babin, *Settlement Spotlights Upstart N.Y. Regulator*, NPR (Aug. 18, 2012, 2:12 AM), http://www.npr.org/2012/08/18/159066054/settlement-shines-light-on-n-y-regulator-agency; Silver-Greenberg, *supra* note 5.

8. MICHAEL GRUSON & RALPH REISNER, REGULATION OF FOREIGN BANKS AND AFFILIATES IN THE UNITED STATES 34 (5th ed. 2008).

operate in the United States banking market is significant for foreign banks because it may result in certain operational and regulatory consequences.[9] A branch of a foreign bank operating in the United States is subject to less regulation than a separately incorporated, federally-insured bank subsidiary, which may be why foreign banks often choose to set up their United States operations in this manner.[10] Indeed, there were 214 foreign bank branches in the United States as of December 31, 2007, accounting for 72.5% of all foreign banking assets in the nation.[11]

Foreign banks, whether operating through branches or other corporate forms, have dramatically increased their presence in the United States commercial banking market.[12] As a result, foreign banks have served to expand credit in the United States, promote financial innovation and foreign investment, and enhance the globalization of United States banking markets.[13] The rise of foreign banking activity in the United States, however, prompted Congress to enact a comprehensive federal regulatory structure to govern the operations of foreign banks.[14] Legislation such as the International Banking Act of 1978 and the Foreign Bank Supervision Enhancement Act of 1991 marks a notable trend toward more federal oversight of those foreign banks operating in the United States.[15]

B. INTERNATIONAL BANKING ACT OF 1978

Concerned that foreign banks operating in the United States were not receiving proper supervision from federal regulators, Congress enacted the IBA to create a more adequate legal framework for regulating such banks.[16] Most importantly, the IBA shifted major responsibility for the oversight of foreign banks to the federal level.[17]

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9. *Id.*
10. *See id.* at 37–38.
11. *Id.* at 38.
12. *Id.* at 3.
13. *Id.* at 6.
14. *Id.* at 8.
15. *Id.* at 7. Congress passed other federal statutes regarding the regulation of foreign banking activities in the United States. However, this Comment will discuss only the IBA and the FBSEA, since they are most relevant.
16. *Id.* at 4, 8.
17. John P. Segala, *A Summary of the International Banking Act of 1978*, FRB RICHMOND ECON. REV., Jan./Feb. 1979, at 16, 19.

Indeed, the IBA was "designed to improve federal control over monetary policy" and allow federal regulators to become more involved in supervising the activities of foreign banks in the United States.[18]

Prior to the IBA, it was most common for state banking regulators, rather than federal authorities, to license and supervise foreign banking operations in the United States.[19] After the IBA was enacted, branches and agencies of foreign banks were able to obtain federal licenses from the Office of the Comptroller of the Currency ("OCC"), subjecting them to primary regulation by the OCC, instead of being limited to state licenses and corresponding state regulation.[20] In addition, the IBA provides supervisory authority to several regulators, including the OCC, the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the states.[21] These regulators were able to assert jurisdiction over those foreign banks that operated within its territory, enabling the regulatory authorities to perform examinations and reviews as necessary.[22] Accordingly, foreign banks now must contend with overlapping layers of federal and state regulatory regimes.[23]

C. FOREIGN BANK SUPERVISION ENHANCEMENT ACT OF 1991

Congress renewed its attempt in the late 1980s and early 1990s to establish a meaningful role for federal authorities in foreign bank regulation.[24] As a result, Congress passed the FBSEA in 1991, which introduced new methods of approval and monitoring of foreign banks and created heightened responsibility for the Federal Reserve Board in the regulatory process.[25] In so doing, the FBSEA substantially increased

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18. *See id.* at 20; *see also* GRUSON & REISNER, *supra* note 8, at 10 (explaining that the IBA achieved Congress' desire to establish a "federal presence" in the regulation and supervision of foreign bank activities in the United States).

19. GRUSON & REISNER, *supra* note 8, at 7–8.

20. *See* 12 U.S.C. § 3102 (2006); *see also* GRUSON & REISNER, *supra* note 8, at 9.

21. Segala, *supra* note 21, at 19.

22. *Id.*

23. GRUSON & REISNER, *supra* note 8, at 10.

24. *Id.* In particular, the collapse of Bank of Commerce Credit International led policymakers to question the effectiveness of United States supervision of foreign banking operations. These concerns were amplified after "widespread media accounts of unauthorized lending to Iraq by the U.S. operations of Banca Nazionale del Lavoro." *Id.*

25. *Id.*

the authority federal regulators have regarding foreign banks operating in the United States.[26]

Prior to the FBSEA, a foreign bank needed only to obtain the approval of the state or federal licensing authority to open a branch in the United States.[27] Now, section 202 of the FBSEA requires advance Federal Reserve approval, as well, for a foreign bank to establish any branch in the United States.[28] Pursuant to the FBSEA, the Federal Reserve may only offer approval if the foreign bank operates its non-U.S. business is directly within the field of banking, it is adequately overseen by the appropriate local authorities in its home country, and it provides the Federal Reserve with all materials necessary to conduct a proper assessment of the bank's application.[29]

Section 7(e) of the IBA, which was enacted as part of the FBSEA, permits the Federal Reserve to close any United States office of a foreign bank.[30] In addition, the FBSEA authorizes the Board to examine any foreign bank office, although it is directed to coordinate its examinations with the OCC, Federal Deposit Insurance Corporation ("FDIC"), and state banking authorities whenever possible.[31] This requirement serves to ameliorate the consequences of overlapping jurisdiction and encourages a more unified examination process.[32]

To coordinate the examination process, the Board has worked with several other regulators, including the OCC, the FDIC, the NYSBD, [33] and state authorities.[34] For example, the Federal Reserve Board and the

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26. Stephen J. Field, Scott N. Benedict, & Francoise M. Haan, *New Law Significantly Increases Regulation of Foreign Banks in U.S.*, *reprinted in* FEDERAL SUPERVISION OF FOREIGN BANKS IN THE U.S. 40 (George M. Cohen et al. eds., 1992).

27. GRUSON & REISNER, *supra* note 8, at 11. In practice, most banks obtained only the approval of the state licensing authority because relatively few foreign banks chose to apply for a federal license directly from the OCC. *See id.*

28. 12 U.S.C. § 3105(d)(1) (2006); GRUSON & REISNER, *supra* note 8, at 11; Field, Benedict, & Haan, *supra* note 26, at 41.

29. 12 U.S.C. § 3105(d)(2); GRUSON & REISNER, *supra* note 8, at 11–12.

30. 12 U.S.C. § 3105(e); Field, Benedict, & Haan, *supra* note 26, at 41.

31. 12 U.S.C. § 3105(c)(1)(B)(i). *See* GRUSON & REISNER, *supra* note 8, at 13.

32. *See* 12 U.S.C. § 3105(c)(1)(B); GRUSON & REISNER, *supra* note 8, at 57. Nevertheless, the Federal Reserve is not required to rely on examination reports prepared by the other supervisory authorities. Field, Benedict, & Haan, *supra* note 26, at 43.

33. In 2011, the New York State Banking Department ("NYSBD") and the New York State Insurance Department were merged to create the DFS. *See* Standard Chartered Bank 6 n.8 (NYS Dep't. of Fin. Servs. Aug. 6, 2012).

34. *See* GRUSON & REISNER, *supra* note 8, at 57–58.

FDIC entered into a national agreement in December of 1998 with state banking departments to coordinate state examination activities with those of the Board and the FDIC.[35] The agreement requires states to designate a specific Federal Reserve Bank and FDIC Regional Office to be responsible for examination and supervisory obligations.[36] Foreign banks, therefore, enjoy a single regulatory point of contact for scheduling and planning examinations.[37] In addition, the State Coordination Agreement allows for one state-banking supervisor to coordinate the examination and supervision of a foreign bank licensed in multiple states.[38]

D. STATE REGULATORY AUTHORITY AFTER THE IBA AND FBSEA

While the Federal Reserve gained more regulatory prominence under the FBSEA, the licensing authority, whether the OCC or the state, is still an important part in supervising the operations of those foreign banks within its jurisdiction.[39] While the IBA provided foreign banks with the option of applying for a federal or state license, most foreign banks still choose to obtain a license from the state in which they reside.[40] This choice reflects a bank's decision to submit to primary regulation by the state rather than federal authorities.[41] Accordingly, state banking regulators license the most foreign banks and have retained a significant amount of power to supervise foreign banks that are operating within their jurisdiction.[42]

E. NEW YORK BANKING LAW

New York Banking Law ("N.Y. Banking Law") requires every licensed foreign banking corporation operating in the state to maintain appropriate documentation of its in-state transactions and transactions involving any other office of the foreign bank that is located outside the

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35. *See id.* at 58.
36. *See id.*
37. *See id.*
38. *See id.*
39. *Id.* at 39.
40. *Id.* at 38.
41. *Id.* at 39.
42. *Id.* at 74.

state.[43] The superintendent of the DFS may examine all of the books, records, and accounts of any agency or branch of a foreign bank located in New York State.[44] The superintendent may also examine any books, records, and accounts of other offices of the foreign bank that are maintained in New York.[45] Because foreign banks have established a significant banking presence in New York,[46] these powers retained by the superintendent are significant.[47] In addition, every foreign bank licensed in the state must prepare written reports describing its asset, liabilities and other pertinent matters as requested by the superintendent.[48]

Foreign banks seeking to open branches in New York must satisfy initial requirements similar to those specified in the FBSEA.[49] For instance, the superintendent must consider the home country's regulatory regime and the extent of that regime's jurisdiction over the bank and whether the bank will be able to provide enough information regarding its operations and activities.[50] In fact, New York amended its application requirements after passage of the FBSEA to more closely parallel those of the Federal Reserve.[51] Furthermore, the superintendent has the power to issue orders directing foreign banking corporations to appear and explain an apparent violation of law, discontinue unauthorized unsafe practices, make good an impairment of the required capital, make good encroachments on required services, and keep books and accounts as prescribed by the superintendent.[52] Notably, the statute lacks any indication that only violations of state law can produce a sanction.[53]

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43. N.Y. BANKING LAW § 200-c (McKinney 2008); 10 N.Y. JUR. 2D *Banks* § 585 (2013).

44. N.Y. BANKING LAW § 36(4); *see also* GRUSON & REISNER, *supra* note 8, at 85.

45. N.Y. BANKING LAW § 36(4); *see also* GRUSON & REISNER, *supra* note 8, at 85.

46. GRUSON & REISNER, *supra* note 8, at 75.

47. *Cf.* Henning, *supra* note 8 (pointing out that Lawsky, as head of the DFS, has unusual powers under the N.Y. Banking Law to affect the operations of a foreign bank).

48. N.Y. BANKING LAW § 204. *See also* 10 N.Y. JUR. 2D *Banks* § 585.

49. GRUSON & REISNER, *supra* note 8, at 77.

50. N.Y. COMP. CODES R. & REGS. tit. 3, Supervisory Policy FB § 1.2 (2013); GRUSON & REISNER, *supra* note 8, at 77.

51. GRUSON & REISNER, *supra* note 8, at 78.

52. N.Y. BANKING LAW § 39. This provision supplied the DFS with the statutory authority to issue the order on August 6, 2012 to Standard Chartered Bank.

53. Henning, *supra* note 8.

II. STANDARD CHARTERED'S SETTLEMENT WITH THE DFS

Part II of this Comment describes the operations and activities of Standard Chartered in the United States. It also discusses Standard Chartered's settlement with the DFS, identifying the issues at stake and introducing the range of responses to the settlement.

A. ACTIVITIES OF STANDARD CHARTERED IN THE UNITED STATES

Standard Chartered is a wholly-owned subsidiary of Standard Chartered PLC, a British bank with a strong international presence.[54] Licensed to operate in New York State,[55] Standard Chartered PLC offers many products and services to its clients, including its dollar clearing operations, which add substantially to Standard Chartered PLC's revenue.[56] The United States Government, through the Office of Foreign Assets Control ("OFAC"), regulates these dollar clearing operations by imposing sanctions against those who attempt to use the United States' financial system in contravention of United States foreign policy or present a threat to national security such as Iran, North Korea, and the Sudan.[57] From 2001 to 2010, Standard Chartered allegedly engaged in dollar clearing transactions with Iran called "U-Turns", which were permitted for some time under limited circumstances and with close regulatory supervision.[58] In November 2008, however, the United States Treasury Department revoked authorization for "U-Turn" transactions with Iran due to concerns that Iranian banks were using that money to purchase nuclear weapons.[59]

In an order issued on August 6, 2012, the DFS accused Standard Chartered of designing and implementing an elaborate scheme to clear illegal transactions in U.S. dollars with Iran by using its New York branch as a front for the prohibited dealings.[60] According to the DFS, these dealings with Iran threatened peace and stability internationally.[61] Among the violations of law propounded by the DFS were

54. *See* Order Pursuant to N.Y. Banking Law § 39, *supra* note 1, at 1, 5.
55. *Id.* at 2.
56. *Id.* at 5, 6.
57. *Id.*
58. *Id.* at 7–8.
59. *Id.* at 8.
60. *Id.* at 2.
61. *Id.* at 22.

"unauthorized transactions" pursuant to 31 C.F.R. 560.516, which was promulgated by OFAC and regulates the transfer of funds involving Iran.[62] According to the DFS, any banking institution that engages in "unauthorized transactions" is unsafe and unsound.[63]

B. THE SETTLEMENT

On August 14, 2012, the DFS and Standard Chartered agreed to settle.[64] Both entities agreed that the transactions were worth at least $250 billion.[65] The settlement included the following terms: Standard Chartered was obligated to pay a civil penalty of $340 million to the DFS, install a monitor for two or more years to ensure that appropriate money-laundering risk controls and corrective measures are firmly in place in the New York branch, and permanently install personnel to ensure that the bank's compliance with due diligence and monitoring requirements.[66]

Commentators agree that the settlement was a "victory" for Benjamin Lawsky and the DFS, which confronted the bank without any involvement of federal regulators;[67] however, some federal authorities were concerned that the deal could compromise their abilities to reach settlements with the bank.[68] Indeed, the actions also perturbed British authorities who felt that Lawsky was spoiling their banks' reputation.[69] In his defense, Lawsky explained that he was pressured to act in the face of Standard Chartered's continuing breach of compliance measures regarding bank secrecy and money-laundering.[70]

In any case, the $340 million fine was an enormous sum for a single state regulator to reap from a settlement with a foreign bank.[71] Banking industry officials have said that this type of occurrence—a state regulator, acting on its own, threatens to take away the state license of a global bank and then secures a public settlement of this magnitude—is

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62. *Id.* at 25.
63. *Id.* at 22.
64. Press Release, Dep't of Fin. Servs., *supra* note 3.
65. *Id.*
66. *Id.*
67. *See* Silver-Greenberg, *supra* note 5.
68. *Id.*
69. *Id.*
70. *Id.*
71. *Id.*

unprecedented;[72] however, there is a reason why the DFS was able to take the lead in the case against a multinational financial institution rather than adhering to the ordinary procedure and deferring to federal regulators and prosecutors.[73] In most cases, a state banking regulator is not able to exert much control over foreign banks.[74] The dynamics of this situation were different, however, because the DFS oversees bank operations in New York.[75] As New York stands as the American financial hub, a foreign bank seeking to do business in the U.S. is virtually required to perform its transactions in the state.[76] Therefore, the DFS had the rare ability to affect the business of a foreign bank with only minor operations in the United States.[77] Furthermore, because the scope of Section 39 of the N.Y. Banking Law is not limited to violations of state law, Lawsky possessed the legal authority to accuse Standard Chartered of violating federal law prohibiting certain dealings with Iran.[78]

C. ISSUES ARISING FROM THE SETTLEMENT

Lawsky's claim that Standard Chartered violated state law by concealing pertinent information from American investigations enabled him to achieve a grand settlement.[79] Nonetheless, critics point to two major problems with this approach. First, the Department of Justice was in the midst of deciding not to file criminal charges just prior to DFS's actions, after concluding that the Iranian transactions substantially complied with federal law.[80] And second, DFS failed to include any federal regulators in its investigation and subsequent action against the bank.[81] In fact, the DFS appeared to intentionally keep the federal

72. Babin, *supra* note 7.
73. *See* Henning, *supra* note 6.
74. *Id.*
75. *Id.*
76. *Id.*
77. *Id.*
78. *Id.*
79. Silver-Greenberg, *supra* note 5.
80. *Id.*
81. *Id.* Lawsky has been unapologetic in his approach, despite the widespread criticism he has faced. *Id.*

authorities in the dark once it commenced its investigation of Standard Chartered.[82]

There is another significant issue raised by the settlement with the DFS. A New York State banking license is necessary for banks doing business with United States currency.[83] Trades in United States currency must be cleared through the United States, and this effectively means that such trades must be processed in New York, because that is where the nation's financial institutions are primarily located and where the most important banking transactions typically occur.[84] Therefore, it is impossible to tell whether Standard Chartered actually settled with the DFS on the grounds that it egregiously violated state and federal laws or whether the settlement was a result of intense pressure levied by the unusually powerful position of a New York State regulator.[85] In other words, the settlement may have been more a representation of the potential costs of a DFS sanction involving the revocation of Standard Chartered's license and not the scope Standard Chartered's illegal acts.[86]

Finally, and more generally, the Standard Chartered settlement illustrates the problems associated with the growth in overlapping layers of federal and state regulation.[87] This expansion has forced banks to confront a "prosecutorial maze" when defending against alleged violations of banking law.[88] In practice, banks operating in the United States may be subject to examination by different branches of one federal agency as well as other federal and/or state regulators.[89] Moreover, the termination of an investigation by one agency does not mean that another will discontinue its own investigation and possible enforcement measures.[90] While these overlaps could be minimized by means of inter-regulatory coordination,[91] the Standard Chartered case

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82. Babin, *supra* note 7.

83. Tim Worstall, *Did Standard Chartered Settle With the DFS? Or Were They Mugged by It?*, FORBES (Aug. 15, 2012, 8:53 AM), http://www.forbes.com/sites/timworstall/2012/08/15/did-standard-chartered-settle-with-the-dfs-or-were-they-mugged-by-it/.

84. *Id.* (explaining that a New York State banking license is essential for any bank conducting business in U.S. dollars).

85. *Id.*

86. *Id.*

87. *The Prosecutorial Maze*, THE ECONOMIST, Oct. 13, 2012, *available at* http://www.economist.com/node/21564563.

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.*

illustrates that meaningful communications among agencies are often lacking, undermining regulatory efficiency.

D. Positive Responses to the Settlement

The DFS settlement with Standard Chartered challenged the ordinary regulatory paradigm in which state regulators cower behind the Federal Reserve, the Treasury Department, and the Department of Justice,[92] but one could argue that what occurred in this case actually served to benefit the public.[93] The fact that federal regulators were compelled to seek larger penalties for their own settlements with Standard Chartered can be seen as a positive.[94] In fact, having an active, competent, functional state regulator can only be beneficial because it would force the federal government to better oversee, rather than protect, large banks.[95]

The settlement also undermined Standard Chartered's assertion that it had conducted only $14 million of illegal transactions with Iran.[96] Although Lawsky estimated the figure at $250 billion, the $340 million deal appears to vindicate the DFS's claims that the illegal transactions were worth far more than $14 million.[97] In addition, one could argue that Lawsky and the DFS had clear jurisdiction over the matter because it involved violations of state law.[98] If the crux of the allegations were that Standard Chartered lied to the DFS about complying with an agreement to correct deficiencies in its anti-money-laundering systems and that Standard Chartered lied in its books and records about its transactions with Iran, then N.Y. Banking Law empowers the DFS to bring such an action against a foreign bank.[99] Ultimately, one could point to the federal government's lackluster job of overseeing large banks and argue that someone needed to step in and be forceful for once.[100] That someone was Benjamin Lawsky, a former federal

92. Weil, *supra* note 6.
93. *Id.*
94. *Id.*
95. *Id.*
96. *Id.*
97. *See id.*
98. *Id.*
99. *Id.*
100. *See id.*

prosecutor who was willing to step up and promote justice by penalizing those institutions that violated federal and state laws.[101]

E. NEGATIVE RESPONSES TO THE SETTLEMENT

Critics of the DFS settlement with Standard Chartered point out the difficulties inherent in a state agency asserting authority over federal issues. Since the DFS is not a federal agency, like the Federal Reserve or the Department of Justice, it does not account for the interests of the entire nation or the means of interstate trade.[102] In addition, the DFS interfered in a matter involving United States foreign relations,[103] traditionally reserved for the federal government.[104] Therefore, the DFS engaged in part in the regulation of banking activity without any specific relevance to New York State.[105]

Some critics focus on the DFS's use of coercion to force the settlement upon Standard Chartered. Since Standard Chartered neither admitted nor denied fault in its settlement agreements and since settlement talks are confidential, whether the bank settled because it actually committed the violations or because it merely sought to lessen its reputational damage and prolonged press coverage will, in all likelihood, never be publicly known.[106] The bank faced serious charges from a critical regulator and the potential loss of its license to operate in New York, which would have devastated its operations and revenue.[107] Therefore, if Standard Chartered agreed to the settlement only because it felt that it had no other choice, then the DFS could be seen as extracting payments through threats,[108] which is an improper government agency action.[109] Of notable focus is the risk to Standard Chartered's reputation resulting from the DFS's actions.[110] Standard Chartered's stock price dropped 22% after Lawsky announced the accusations on August 6,

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101. *See generally id.*
102. Sundaresan, *supra* note 6.
103. *Id.*
104. *Id.*
105. *Id.*
106. *See An Unsettling Settlement: Standard Chartered Douses Incendiary Accusations by Paying a $340M Fine*, THE ECONOMIST, Aug. 18, 2012, http://www.economist.com/node/21560583.
107. *See id.*
108. *Id.*
109. *Id.*
110. *See id.*

2012.[111] Although the settlement allowed the bank's management to avoid censure and continue operating in the United States, Standard Chartered's worldwide reputation has been impaired.[112]

The DFS and New York Governor Andrew Cuomo may also be perceived as having aggressively pursued the settlement solely to enhance their own reputational and financial postures.[113] Indeed, Governor Cuomo responded to the settlement by praising himself for creating the DFS.[114] In addition, the settlement money will flow to the State of New York, thereby benefitting New Yorkers.[115] Another major concern involves Lawsky's decision to move independently of federal regulators, effectively shielding the federal government from the DFS investigation and subsequent negotiations with Standard Chartered. Specifically, the actions by Lawsky and the DFS created a problem for the federal government's own investigations of the bank.[116] Because Lawsky caught the Federal Reserve and the Department of Justice off guard by accusing the bank of misconduct, the federal regulators found themselves tasked with determining the course of their investigations far sooner than they would have liked.[117]

Finally, Lawsky's "lone ranger" move against Standard Chartered has created uncertainty among several global banks.[118] The DFS's money laundering allegations have caused global banks to worry that their New York operations could make them public targets for transactions that federal regulators already decided were legal.[119]

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111. *Id.*

112. *Id.*

113. *See id.* ("The deal gives the DFS a notable scalp, not to mention a considerable financial boost.").

114. *Id.*; *see also* Silver-Greenberg, *supra* note 5 (referring to Governor Cuomo's staunch support for the creation of the DFS as a "modern regulator for today's financial marketplace").

115. Silver-Greenberg, *supra* note 5.

116. Henning, *supra* note 6.

117. *Id.*

118. *See* Jessica Silver-Greenberg, *Accusations Facing Bank Cast a Chill*, N.Y. TIMES, Aug. 11, 2012, at B1, *available at* http://www.nytimes.com/2012/08/11/business/standard-chartered-case-casts-a-chill-over-the-industry.html.

119. *Id.* In a number of settled money-laundering cases with several European banks, such as Lloyds, Barclays, and ING, the Department of Justice and the New York County District Attorney's Office did not object to the "U-Turn" transactions with Iran that occurred before the Treasury Department issued its new ruling in November 2008. *Id.*

Indeed, federal law enforcement officials have received numerous calls from bank executives who were worried that the rules regarding Standard Chartered's disputed financial transactions have suddenly changed.[120] Therefore, banks may be forced to institute new plans to deal with the apparent divergence between state and federal law.[121]

III. RECOMMENDATIONS FOR RESOLVING THE ISSUES ARISING FROM THE DFS SETTLEMENT

Part III of this Comment introduces a framework for mitigating the overarching problems associated with overlapping regulatory jurisdiction among state and federal authorities. As an initial matter, it analyzes the consequences of the DFS settlement. Then, it discusses how the principle of comity in the context of vertical federalism should serve to alleviate the negative results of overlapping regulatory jurisdiction. In doing so, this Comment argues that state and federal regulators should be required to communicate when pursuing potential violations, and deference should be granted to either the state or federal regulator depending on whether the foreign bank primarily violated state or federal law. This Part further explains that in such a scenario, federal regulators should have primary authority to enforce federal law violations against foreign banks, and state regulators should be afforded primary authority to enforce violations of state law. As an alternative, Part III also proposes amending federal legislation regarding the regulation of foreign banks to require greater coordination—in a sense, establishing mandatory, rather than voluntary, comity rules—between state and federal regulators when responding to violations of law committed by a foreign bank.

A. SHOULD A STATE REGULATOR ENFORCE FEDERAL LAWS AGAINST A FOREIGN BANK?

The DFS's settlement with Standard Chartered raises major concerns regarding the extent to which a state regulator should be enforcing federal law against a foreign banking corporation.[122] The DFS

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120. *Id.*

121. *Id.* (noting the confusion among many bank executives as to whether the banking rules have changed).

122. *See* Henning, *supra* note 6 (noting that the DFS based its case, at least in part, on Standard Chartered's possible violations of federal law regarding the bank's reporting of transactions with Iran); *see also* Sundaresan, *supra* note 6 (disparaging the

Order dated August 6, 2012 provides numerous references to federal issues concerning the United States Government. For instance, the "Preliminary Statement" accuses the bank of engaging in "deceptive and fraudulent misconduct" on behalf of Iranian financial institutions "that were subject to U.S. economic sanctions."[123] Furthermore, the DFS accused Standard Chartered of undertaking a course of conduct that included "evading Federal sanctions."[124] In describing the bank's illegal conduct, the DFS explained that "the U.S. Government administers and enforces a sanctions regime against those who attempt to use the U.S. financial system in contravention of U.S. foreign policy and those foreign countries, entities, and individuals who may present a threat to national security."[125] Finally, under the section entitled "Apparent Violations of Law," the DFS accused Standard Chartered of engaging "in transactions within the United States without complying with the requirements of 31 C.F.R. 560.516,"[126] a federal regulation.

Although Section 39 of the N.Y. Banking Law authorizes the DFS's superintendent to impose sanctions for federal law violations, this authority creates a serious problem when state and federal regulators are intent on enforcing federal laws differently.[127] The DFS settlement illuminated this problem specifically because federal regulators were on the verge of concluding that all of Standard Chartered's transactions complied with federal law.[128] Therefore, banks worried that the DFS's interpretation of Iranian sanctions would undermine any the assurances from federal regulators that their actions were legal.[129]

While the ability of a state regulator to enforce federal law against foreign banks may mitigate federal inaction, the divergence of state and

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DFS for attempting to regulate activity without any specific relevance to the territory of New York).

123. *See* Order Pursuant to N.Y. Banking Law § 39, *supra* note 1, at 2.

124. *Id.* at 3.

125. *Id.* at 6.

126. *Id.* at 25.

127. *See* Silver-Greenberg, *supra* note 118 (describing the concern among banks that state and federal regulators are interpreting the law in different ways); *see also* Henning, *supra* note 6 (noting that federal regulators were forced to decide whether to go forward with their own investigations far sooner than they would have liked as a result of Lawsky's order).

128. *See* Silver-Greenberg, *supra* note 118.

129. *See id.* ("[F]ederal law enforcement officials have been fielding a flurry of worried calls from bank executives concerned that the rules have suddenly changed . . . .").

federal regulators creates a level of uncertainty among the banking community that can be far more devastating to the national banking system. When banks do not understand the rules, they hesitate to perform the transactions affected by those rules.[130] When banks refuse to engage in certain financial transactions, they may fail to provide the services necessary to stimulate and maintain a healthy national economy.[131] In order to avoid this uncertainty and the resulting consequences, state regulators should step aside to allow federal regulators to maintain responsibility for enforcing federal law against foreign banking organizations.[132]

The principle of comity serves to ameliorate the problems arising from concurrent regulatory jurisdiction over foreign banks. Following the traditional notion of judicial comity, courts give effect to the laws and judicial systems of another state or jurisdiction as a matter of practical deference, although they hold no actual obligation to do so.[133] The principal of comity is based on a mutual respect between jurisdictions.[134] It is not a rule of law; rather, it is a voluntary expression of deference to the policy of another jurisdiction, particularly where that jurisdiction asserts a strong interest in the matter.[135] The principle is "grounded in notions of accommodation and good-neighborliness," and serves to promote balance and harmony among various state and federal tribunals.[136]

The benefits of promoting comity in the regulatory sphere are particularly evidenced when—as was the case with Standard

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130. *See generally* Alison M. Hashmall, Note, *After the Fall: A New Framework to Regulate "Too Big to Fail" Non-Bank Financial Institutions*, 85 N.Y.U. L. REV. 829, 843–44 (2010) (explaining that uncertainty can result in declined lending and investment activity).

131. *See* generally *id.* at 844 (noting that declined lending and investment activity can "exacerbate or even trigger panic and financial crises").

132. *See generally* Sundaresan, *supra* note 6 (suggesting that federal regulators should have exercised their jurisdiction over the alleged violations committed by Standard Chartered, rather than the DFS, because they would have properly considered "the interests of the entire nation and means of inter-state trade").

133. *See* Rhines v. Weber, 544 U.S. 269, 274 (2005).

134. *See* Sean J. Griffith & Alexandra D. Lahav, *The Market for Preclusion in Merger Litigation*, 66 VAND. L. REV. 1053, 1116 (2013).

135. Boudreaux v. State of La., Dep't of Transp., 897 N.E.2d 1056, 1059 (2008); *see also* Thompson v. City of Atlantic City, 921 A.2d 427, 441 (2007) ("Comity is practiced when a court of one jurisdiction voluntarily restrains itself from interfering in a matter falling within the purview of a court of another jurisdiction.").

136. *Thompson*, 921 A.2d at 441.

Chartered—the thrust of the claims asserted by regulators derives from a federal law prohibiting certain transactions with a foreign nation.[137] In this situation, it seems proper based on comity for the state regulator to defer to federal regulators, thereby supporting a coherent and accurate administration of the federal law.[138] Adherence to the principle of comity could create a more harmonious atmosphere between state and federal authorities, and promote efficient regulation of foreign banks operating in the United States.[139]

B. SHOULD A STATE REGULATOR BE ABLE TO ACT INDEPENDENTLY OF FEDERAL REGULATORS?

While state regulators may often be involved in investigations of foreign banks, the case of Standard Chartered was unique in that state regulators usually do not take the lead in cases involving multinational financial institutions.[140] Instead of deferring to federal regulators and prosecutors, Lawsky and the DFS moved swiftly on their own against the bank.[141] Although an active state regulator can be an integral part of an overarching investigation of foreign banks, problems develop when state and federal regulators fail to coordinate.[142] This precise problem occurred in the DFS settlement.[143]

Federal regulators, along with the general public, were blindsided by Lawsky's aggressive actions against Standard Chartered.[144] Indeed, the DFS accusations and resulting settlement compelled federal

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137. *See* Sundaresan, *supra* note 6 (explaining that the alleged Standard Chartered violations centered around circumvention of U.S. sanctions against Iran).

138. *See generally id.* (suggesting that federal regulators would have properly considered the interests of the entire nation in deciding how to apply a federal law to a foreign bank).

139. *See* Allan Erbsen, *Horizontal Federalism*, 93 MINN. L. REV. 493, 569 (2008) (explaining how the principle of comity can help avoid interstate friction in the context of horizontal federalism by restraining aggressive assertions of authority).

140. *See* Henning, *supra* note 6.

141. Babin, *supra* note 7 (discussing how Lawsky and the DFS moved forward against Standard Chartered without the involvement of federal regulators).

142. *See* Silver-Greenberg, *supra* note 118 (discussing how the strong accusations by the DFS created confusion among banks, which were relying on prior decisions by federal regulators, as to the legality of certain financial transactions).

143. *See id.*

144. *See* Henning, *supra* note 6 ("Lawsky caught the Federal Reserve and the Justice Department off guard by accusing the bank of misconduct.").

regulators to decide the course of their investigations sooner than they would have liked.[145] The federal regulators, such as the Federal Reserve and the Department of Justice, also lost a valuable negotiating tactic as a result of Lawsky's actions.[146] By failing to move in concert with other regulators, the DFS jeopardized the federal regulators' ability to reach a comprehensive settlement with Standard Chartered that could have settled all of the investigations.[147] Accordingly, the federal regulators may have subsequently found it more difficult to extract substantial money payments from Standard Chartered since the bank had already agreed to pay $340 million to the DFS.[148]

To prevent this type of "lone-ranger" move by a state regulator, the principle of comity must control. Mutual respect that is the basis of comity should require state and federal regulators to maintain an open dialogue regarding their enforcement strategies,[149] and state and federal regulators should be communicating openly about their plans to investigate or bring an enforcement action against a foreign bank.[150] This could be achieved if regulatory authorities provide notice to those with concurrent jurisdiction of when they plan either to hold a hearing or file claims against a foreign bank.[151] Had this requirement been in force, the DFS would not have been able to covertly pursue Standard Chartered, and thereby catch the federal regulators off-guard.

Alternatively, Congress could decide to amend the IBA to make comity mandatory among state and federal regulators of foreign

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145. *Id.* (noting that federal regulators were hastily placed "in the uncomfortable position of deciding what to do with their investigations").

146. *See id.* (explaining how the DFS case had the potential to jeopardize the federal investigations of Standard Chartered).

147. *See id.*

148. This point is bolstered by the fact that Standard Chartered agreed on December 10, 2012 to pay $327 million in fines to federal authorities, which is even *less* than what the DFS, as a single state regulator, was able to extract from the bank. *See* Howard Mustoe, *Standard Chartered Pays $327 Million on U.S.-Iran Transfers*, BLOOMBERG (Dec. 10, 2012, 12:33 PM), http://www.bloomberg.com/news/2012-12-10/standard-chartered-pays-327-million-in-u-s-iran-transfers-case.html.

149. *See generally* Griffith & Lahav, *supra* note 134, at 1116 (explaining that cross-jurisdictional communication among judges may alleviate problems arising from multi-forum litigation).

150. *Cf. id.* (advocating for open dialogue among judges presiding over rival jurisdictions in order to strengthen inter-state relations).

151. *See id.* at 1126–31 ("Notice is a first step to promoting comity.").

banks.[152] Such an amendment might induce greater coordination among state and federal regulators by strengthening existing voluntary comity rules, or by threatening those regulators who make overly aggressive assertions of authority with judicial intervention.[153] For example, although Section 3105 of the IBA provides for coordination of foreign bank examinations,[154] it might also require coordination of enforcement actions against those banks.[155] If this had been adopted, the DFS may not have been able to act independently of federal regulators in accusing Standard Chartered of violating state and federal law.[156] Rather, the state and federal authorities could have worked together to reach a potentially sweeping settlement with the bank that could have settled matters definitively for all parties involved.

C. SHOULD A STATE REGULATOR BE INVOLVING ITSELF IN ISSUES OF FOREIGN POLICY?

By accusing Standard Chartered of violating United States sanctions against Iran, the DFS involved itself in issues of American foreign policy. The relevant sanctions, administered by the United States Government through the OFAC, aims to prevent "those who attempt to use the United States financial system in contravention of United States foreign policy and those foreign countries, entities, and individuals who may present a threat to national security."[157] In the case of Iran, the United States Treasury Department revoked authorization for the "U-Turn" transactions that Standard Chartered allegedly processed because it suspected Iran of leveraging the transactions to finance the Iranian nuclear weapons program.[158] Lawsky clearly

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152. *Cf.* Erbsen, *supra* note 139, at 569 ("Mandatory comity rules might also lead states to avoid conflict by strengthening their existing voluntary comity rules . . . .").

153. *See id.* (discussing how a constitutional common law of comity might help avoid inter-state friction).

154. *See* 12 U.S.C. § 3105(c)(1)(B)(i) (2006).

155. This type of stronger coordination is both practical and reflects the legal principle of comity. *America's Financial System: Law and Disorder*, THE ECONOMIST, Oct. 13, 2012, *available at* http://www.economist.com/node/21564565.

156. Although state and federal regulators have entered into various coordination agreements with regard to state *examination* activities, *see supra* notes 35–38 and accompanying text, these agreements do not include any provisions regarding coordinated *enforcement* among state and federal regulators.

157. *See* Order Pursuant to N.Y. Banking Law § 39, *supra* note 1, at 6.

158. *Id.* at 8.

understood the foreign policy implications of his allegations against Standard Chartered.[159] He specifically accused the bank of designing and implementing "an elaborate scheme by which to use its New York branch as a front for prohibited dealings with Iran—dealings that indisputably helped sustain a global threat to peace and stability."[160] In fact, Lawsky stated that "[t]his is a case about Iran, money laundering and national security."[161]

The ability of the DFS, as a state regulator, to have such an impact on foreign policy presents both a practical and constitutional problem. Practically speaking, a New York regulator is charged with protecting the interests of New York State, not the United States as a whole.[162] Federal regulators must, however, consider the interests of the entire nation and means of inter-state trade before deciding whether to pursue a foreign bank allegedly violating United States sanctions against a foreign nation.[163] Federal regulators, thus, may have weighed the negative impact on international relations and foreign trade in deciding not to pursue claims against Standard Chartered initially.[164] By bringing such bold accusations and securing such a grand and public settlement against Standard Chartered, however, the DFS was able to assert just as large of an influence on foreign relations without considering the interests of the entire nation.[165] Had the DFS worked more closely with federal regulators, Lawsky may have been more hesitant to move against Standard Chartered, and the state and federal regulators, working in concert, may have been able to reach a more prudent decision, taking into account the interests of the United States as a whole.

Constitutionally, a state regulator's ability to make decisions affecting foreign policy may undermine federal supremacy. The United States Constitution vests the federal government with the power to

159. *See generally id.* at 22 (accusing Standard Chartered of engaging in prohibited dealings with Iran "that helped sustain a global threat to peace and stability"); Weil, *supra* note 6 (noting that British officials were especially upset by Lawsky's treatment of Standard Chartered).

160. *See* Order Pursuant to N.Y. Banking Law § 39, *supra* note 1, at 22.

161. Silver-Greenberg, *supra* note 118, at 3.

162. *See* Sundaresan, *supra* note 6 (suggesting that a New York agency should be confined to regulating banking activity that has a specific relevance to the territory of New York).

163. *See id.* (explaining that federal regulators would look at the interests of the entire nation and means of inter-state trade before making a determination regarding potential violations committed by a foreign bank).

164. *See id.*

165. *See id.*

regulate commerce with foreign nations.[166] When Congress passes a law regulating commerce with foreign nations, the executive branch must faithfully execute it.[167] Therefore, it is the United States Government, through the OFAC, that has the ability to administer and enforce a sanctions regime against Iran.[168] By virtue of the Supremacy Clause,[169] a New York State regulator should not be able to make foreign policy decisions that run counter to those made by the United States Government.[170] By enforcing United States sanctions against a foreign bank, the DFS made a decision influencing foreign policy that federal regulators, as representatives of the United States Government, should have made instead.[171]

A state regulator's ability to enforce a federal law related to foreign relations implicates the principle of comity, but here, international comity among nations as well. The Restatement (Third) of Foreign Relations Law ("the Restatement") defines the parameters of comity among nations with respect to the states, and focuses specifically on a state's ability to exercise jurisdiction to prescribe law with respect to a person or activity having connections with another state.[172] According to the Restatement, a state has jurisdiction to prescribe law with respect to conduct that takes place within its territory.[173] However, Section 403 prohibits a state from prescribing law with respect to a foreign entity, whether or not the conduct took place within its territory, when the exercise of such jurisdiction is unreasonable.[174]

Whether an exercise of jurisdiction over a person or activity is unreasonable depends on a number of relevant factors.[175] Application

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166. U.S. CONST. art. I, § 8, cl. 3.

167. U.S. CONST. art. II, § 3. In this case, the executive branch's power to execute the laws passed by Congress is performed by the federal regulators, as part of the administrative state.

168. *See* 31 C.F.R. § 560.516 (2012).

169. U.S. CONST. art. VI, cl. 2.

170. *See* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 402 note 5 (2012) ("Under United States laws, any exercise of jurisdiction to prescribe by a State is subject to applicable Constitutional limitations, notably Article I, Section 10, and to the supremacy of United States treaties and laws.").

171. *See* Sundaresan, *supra* note 6.

172. *See* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 403(1).

173. *Id.* § 402(1)(a).

174. *See id.* § 403(1).

175. *Id.* § 403(2)(a)–(h). These factors include the following:

of these factors suggests that it is unreasonable for a New York State authority to be involved in the regulation of a foreign bank's transactions with Iran.[176] First, the character of the activity to be regulated, as discussed, involves issues of foreign policy, which traditionally are reserved for the federal government.[177] Second, the justified expectations of foreign banks have been hurt by the DFS involvement because the banks reasonably expected, on the basis of the federal regulators' consensus, that the transactions they engaged in were legal.[178] Third, state regulation of a foreign bank's transactions with Iran appear unimportant to the international political, legal, or economic system in light of the fact that the federal government is already attuned to the issue.[179] Fourth, state regulation here is inconsistent with the traditions of the international system because "[i]nternational law and international agreements of the United States are law of the United States and supreme over the law of the several States."[180] Fifth, federal regulators have a substantially greater interest in regulating the activity because the dollar-clearing transactions with Iran are proscribed by

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(a) the link of the activity to the territory of the regulating state, i.e., the extent to which the activity takes places within the territory, or has substantial, direct, and foreseeable effect upon or in the territory;
(b) the connections, such as nationality, residence, or economic activity, between the regulating state and the person principally responsible for the activity to be regulated, or between that state and those whom the regulation is designed to protect;
(c) the character of the activity to be regulated, the importance of the regulation to the regulating state, the extent to which other states regulate such activities, and the degree to which the desirability of such regulation is generally accepted;
(d) the existence of justified expectations that might be protected or hurt by the regulation;
(e) the importance of the regulation to the international political, legal, or economic system;
(f) the extent to which the regulation is consistent with the traditions of the international system;
(g) the extent to which another state may have an interest in regulating the activity; and
(h) the likelihood of conflict with regulation by another state.
Id.

176. There is a link between the activity of Standard Chartered and the territory of the regulating state, since the dollar-clearing transactions did take place in New York; however, application of the remaining factors demonstrates the unreasonableness of a state regulator's ability to regulate a foreign bank in this case.

177. *See* Sundaresan, *supra* note 6.

178. *See* Silver-Greenberg, *supra* note 118.

179. *See generally* Sundaresan, *supra* note 6.

180. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 111(1).

federal not state law.[181] And finally, the DFS's involvement with Standard Chartered has resulted in a conflict with regulation by the federal authorities, creating confusion among foreign banks operating in the United States with regard to the legality of certain "U-Turn" transactions.[182] Accordingly, the DFS should not have exercised jurisdiction over Standard Chartered's alleged failure to comply with federal law regarding illicit transactions with Iran.

D. Should a State Regulator Be Involved in the Regulation of a Foreign Bank Operating in the United States At All?

Admittedly, there are some benefits to allowing a state regulatory authority to examine and enforce violations of law against a foreign bank operating in its state. For one, it would seem odd to permit state authorities such as the DFS to regulate state and national banks[183] operating within its territory, but not allow those authorities to regulate the foreign banks operating there.[184] After all, the state government is charged with protecting the interests of its citizens, so it should be able to regulate the activity of any bank that is operating on its turf.[185] Furthermore, if a foreign bank is violating only state law, federal regulators will not be inclined to intervene to enforce the law and impose penalties.[186] In addition, even if a foreign bank is violating a federal law, a state regulator's action may prompt federal regulators to confront the matter, effectively providing an incentive for federal

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181. *See* 31 C.F.R. § 560.516 (2012).

182. *See* Silver-Greenberg, *supra* note 118.

183. The National Bank Act, as codified at 12 U.S.C. § 484 (2006), "generally places national banks under federal regulatory control, with a limited exception for states to enforce their own unclaimed property or escheat laws." Louis P. Malick, Note & Comment, *Cuomo v. Clearing House Association, L.L.C.: States Enforcing State Laws Against National Banks*, 6 J. BUS. & TECH. L. 487, 495 (2011) (explaining that the Act shields national banking from unduly burdensome and duplicative state regulation).

184. *See generally* GRUSON & REISNER, *supra* note 8, at 74 (noting that the federal statutes providing for the regulation of foreign banks allow state banking authorities to retain a significant role in supervising foreign banks operating within their territory).

185. *See* Sundaresan, *supra* note 6 (suggesting that perhaps there would be no issue with the actions of the DFS if the alleged violations committed by Standard Chartered had some specific relevance to the territory of New York).

186. *Cf.* Weil, *supra* note 6 (suggesting that federal regulators often act complacently even in the face of violations of *federal* law).

regulators to more aggressively enforce violations of law and do a better job of overseeing large banks.[187]

However, these benefits must be weighed against the negative consequences, described above, that were implicated by the DFS settlement with Standard Chartered. By allowing the states to regulate foreign banks only to the extent that they are violating state law, the benefits of state regulation largely will remain intact.[188] And indeed, the principle of comity also suggests that federal authorities should defer to the jurisdiction of state authorities over an issue derived almost entirely from state law.[189] In such a situation, the state government would be able to protect the interests of its citizens by holding foreign banks accountable for violations of state law.[190] In addition, a state regulator's action against a foreign bank for violations of state law may serve to induce action on the part of federal regulators if the bank is also violating federal law.[191] Simultaneously, by encouraging states to defer to federal regulators when enforcing violations of federal law, the negative consequences of state regulation of foreign banks will be reduced.[192] Had this requirement been in place, the federal authorities would have taken control of the Standard Chartered case, and the DFS would have been unable to create the atmosphere of confusion among global banks and tension with foreign nations that resulted from its own settlement with Standard Chartered.

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187. *See id.*

188. Although the DFS did base several of its accusations on violations of state law, such as the failure to maintain accurate books and records and the falsification of books and reports, these violations were an afterthought to the more general allegation that Standard Chartered violated federal sanctions against Iran. In other words, all of the state-law claims asserted were based upon Lawsky's paramount claim that the bank violated federal law. In cases such as this, where the underlying cause of action derives from the bank's violation of federal law, the state regulator should defer to federal authorities.

189. *See* New York *ex rel.* Cuomo v. Dell, Inc., 514 F. Supp. 2d 397, 401 (N.D.N.Y. 2007) (explaining that the principles of comity and federalism prevent the exercise of federal jurisdiction where the case involves almost entirely an issue of state law).

190. *See supra* text accompanying note 186.

191. *See supra* text accompanying note 187.

192. It has been proposed, instead, that federal regulators should supervise national issues, such as international money-laundering, terrorist financing, and tax matters, while state regulators should be responsible for consumer protection. *See The Prosecutorial Maze*, *supra* note 98, at 2. While it is true that this proposal may have alleviated some of the problems raised by the DFS settlement, it does not serve to minimize regulatory overlap in cases where the state regulator is enforcing a federal law that deals with domestic or seemingly local issues. *See supra* Part II.C.

CONCLUSION

The legal principle of comity suggests that for various practical reasons, a state regulator should defer to the jurisdiction of federal authorities when a foreign bank is accused of violating federal law. That deference should reflect a mutual respect between state and federal regulators that, ultimately, would minimize issues arising from overlapping regulation and promote regulatory efficiency. In the alternative, the IBA should be amended to require greater coordination between state and federal regulators examining and enforcing the law against foreign banks by imposing a mandatory comity requirement. In effect, this would reduce the likelihood that a state regulator could act independently and without the interests of the entire nation in mind when deciding to assert claims against a foreign bank. This approach attempts to balance the benefits of state regulation of foreign banks with the potentially calamitous consequences resulting from such regulation when, as in the case with Standard Chartered, a state regulator seeks to impose sanctions against a foreign bank for violations of federal law.