



CALIFORNIA DEBT AND INVESTMENT ADVISORY COMMISSION

Investments under Government Code 53601– Focus on Securities Issued by Foreign Entities and Foreign Affiliates – 2025 Update

INTRODUCTION

California Government Code contains specific provisions for the types of public investments and investment practices permitted after meeting the broad requirement of preserving principal and maintaining necessary liquidity before seeking yield. While these codes identify the types of permissible investments local agencies may choose when investing surplus funds, a local agency is responsible for ensuring that a security meets the statutory requirements of Government Code at the time of purchase.

With respect to securities issued by affiliates of foreign entities, the Government Code authorizes local agencies to invest in these securities so long as certain statutory conditions are met. In 2013, the California Debt and Investment Advisory Commission (CDIAC) published, “Investments under Government Code 53601(k) – Focus on Foreign Issuers,” which provided a general overview of medium-term notes issued by foreign firms and their affiliates and a brief discussion on how to determine if the issuing entity meets the requirements for investment under the Government Code. Since the publication of the original brief, legislative changes as well as additional online resources have become available to assist local agencies in determining

the permissibility of an investment security issued by a foreign entity.

The purpose of this brief is to assist local agencies in deciding whether an investment product meets the requirements of section 53601 regarding the issuer’s affiliation with a foreign entity. This brief describes different investment types that may be issued by a foreign or foreign affiliated entity and identifies ways local agencies can determine whether the issuer meets the requirements pursuant to Government Code 53601.

WHAT DEBT IS ISSUED BY FOREIGN AND FOREIGN AFFILIATED ENTITIES?

Dollar-denominated debt securities issued by foreign entities in the United States market are often referred to as “Yankee Bonds” or “Yankee CDs”. Although these securities are issued by foreign corporations, banks, and sovereign nations, the Securities and Exchange Commission (SEC) registration requirements are very similar to those for domestic securities. They are rated by a nationally recognized statistical rating organization (NRSRO) and commit to making market disclosures in compliance with securities laws and regulation. However, these characteristics alone are insufficient to determine if California public agencies may invest in these securities.

Currently under California Government Code, there are five types of permissible investment instruments that could be issued by foreign affiliated entities. Permissible medium-term investment options are authorized under sections 53601(k) and 53601(q) which specify the qualifying criteria for medium-term notes and debt obligations issued by supranational organizations. The permissible short-term investments fall

under sections 53601(g), 53601(h) and 53601(i) for bankers’ acceptances, commercial paper and negotiable certificates of deposit, respectively. Table 1 in Appendix A provides a complete summary of the statutory requirements for these sections.

DETERMINING THE ELIGIBILITY OF THE SECURITY’S ISSUER

While understanding an investment security’s rating and portfolio allocation restrictions under Government Code may seem straightforward, the legal and regulatory complexities inherent in the incorporation and licensing status of the issuing entities can present challenges in determining if a specific investment product issued by a foreign or foreign affiliated entity is permissible under section 53601. Investors considering the purchase of securities issued by foreign-affiliated entities may be uncertain about how to apply “*organized*”, “*operating*”, and “*licensed*”, the specific terms contained in section 53601 used to establish the entity’s qualifications as an issuer. The terms “organized”, “operating”, and “licensed” are not specifically defined by statutes nor are they legal terms that hold a specific meaning. However, in the context and use within specific subsections of section 53601, CDIAC interprets these terms as follows.

- **ORGANIZED** – An entity organized as a corporation, special purpose corporation, trust, or limited liability company in the United States.
- **OPERATING** – Being engaged in business activities and maintaining a functioning office (other than a representative office) in the United States.
- **LICENSED** – Permitted by the appropriate regulatory agency to operate and conduct business in the United States (federal license) or a specific state (state license).

To illustrate CDIAC's approach in determining eligibility of securities issued by the affiliates of foreign entities, this brief applies examples involving securities issued by two well-known international companies, Toyota Corporation and Royal Bank of Canada (RBC).

Toyota Corporation is a household name with a large presence in the United States but is incorporated in Japan. Therefore, its securities issued in the United States markets do not meet the "organized" requirement of section 53601(k). In contrast, Toyota Motor Credit Corporation; (the financing arm of Toyota) is incorporated in the United States and satisfies the qualifying criteria requirement as an *organized* corporation in the United States. Therefore, California local agencies may purchase securities issued by Toyota Motor Credit Corporation if the securities meet the other statutory requirements.

A more complex example involves a financial institution. Royal Bank of Canada is a Canadian multinational financial services company which has operations in the United States. One of its subsidiaries is City National Bank, a California-based FDIC-insured bank. Because City National Bank accepts retail deposits, it qualifies as a depository institution as defined by the Federal Reserve System.¹ Licensed by the Office of the Comptroller of Currency (OCC), City National Bank is engaged in banking activities that meet the *licensed and operating* requirements of a depository institution under section 53601(k). However, securities issued by "Royal Bank of Canada" are not allowable investments for California local agencies because it is not a licensed and operating U.S. depository institution under the name of "Royal Bank of Canada", but rather licensed and operating in the U.S. as "RBC Bank". The determination of incorporation, operation, and license status can typically be found through public records such as annual reports, state and federal filings, credit rating reports and the

issuer's own website. In addition, resellers of financial data such as Thomson Reuters and Bloomberg contain data identifying the country and state of incorporation for investment products in their databases.

Identification of the venue for any legal recourse in the event of a bankruptcy or credit event can provide an evaluation of risk and added evidence of an entity's status as organized and operating within the U.S. If the entity's securities are backed by assets that are in the U.S., then investors may attempt to attach a claim on the assets in a United States court in the event of a bankruptcy or default. If the securities are not backed by assets in the United States, then the initial financing documents of the underlying security may provide a possible source to assist with determining the legal venue. While not conclusive, if the venue for legal recourse is outside of the United States, it is less likely that the issuing entity is organized and operating in the U.S. and meets the requirements of section 53601(k) for corporate debt securities.²

Some financial institutions with complex licensing and regulatory characteristics might need additional research and legal interpretation. Local agencies, in consultation with their legal counsel, should establish a procedure for determining if the issuing entity meets the requirements of section 53601 if the issuer is a foreign or foreign affiliated firm.

The following two sections summarize sources of information for verifying an issuer's "organized", "operating", and "licensed" status as these terms apply to affiliates of foreign corporations and affiliate branches of foreign banks and depository institutions.

SOURCES OF INFORMATION ON AFFILIATES OF FOREIGN CORPORATIONS

Is the corporation, special purpose corporation, trust, or limited liability company organized (incorporated) in the United States?

- Search the Securities and Exchange Commission's (SEC) database for corporations reporting to SEC. [SEC.gov | EDGAR | Company Filings](https://www.sec.gov/edgar) If the search result for a specific issuer (corporation, special purpose corporation, trust, or limited liability company) does not indicate a U.S. state as the issuer's state of incorporation, the issuer does not meet the requirements for investment under section 53601(h) and 53601(k).
- If the search of the SEC database for the specific issuer renders no result, as may be the case with a special purpose corporation, trust, or limited liability company, review the Secretary of State websites of the states in which the entity is suspected to be organized.
- If the U.S. organizational status cannot be confirmed by the above sources, local agencies should consult with their counsel and utilize other methods to make the confirmation prior to investment.

Is the corporation operating in the United States?

- This information may not be available at a single source. Check the firm's website and annual reports, Bloomberg, Thomson Reuters, and credit rating reports for the location and organizational structure between a parent company and its U.S. affiliates.

SOURCES OF INFORMATION ON FEDERALLY- AND STATE-LICENSED FOREIGN BANKS AND AFFILIATES

Is the financial institution operating and licensed in the United States?

- Use the National Information Center to review basic information about the entity.³ www.ffiec.gov/nicpubweb/nicweb/NicHome.aspx

¹ The Federal Reserve System defines a depository institution as: "A financial institution that is legally permitted to accept deposits from individuals. Depository institutions include savings banks, commercial banks, savings and loan associations, and credit unions."

² *Local Agency Investment Guidelines, Update for 2025*, CDIAC 24.12, p. 23, www.treasurer.ca.gov/cdiac/LAIG/guideline.pdf, accessed January 2025.

³ The National Information Center, (maintained by the US Federal Reserve System) is a central repository of data about banks and other financial institutions, including both domestic and foreign banking organizations, operating in the United States.

- The Office of the Comptroller of Currency (OCC) charters and regulates national banks and federal savings associations. A list of these entities can be found at: www.occ.gov/topics/licensing/national-bank-lists/index-active-bank-lists.html
- Locate current and former FDIC-insured banking institutions by name, FDIC certificate number, website and/or by location: [BankFind Suite \(fdic.gov\)](http://BankFindSuite(fdic.gov))
- Review the yearly Uniform Bank Performance Report (UBPR) of financial institutions by the Federal Financial Institutions Examination Council. This report would help determine the United States operations of institutions as well as valuable information about the overall financial health of the entity. www.ffiec.gov/ubpr.htm

Is the financial Institution licensed in any state?

- Check for the state bank licensing departments contacts through the Conference of State Bank Supervisors: www.csbs.org/contact-your-state-bank-agency
- In California, The Department of Financial Protection and Innovation regulates and issues licenses for foreign banks agencies and branches: [Licenses and Industries Regulated by the Department | The Department of Financial Protection and Innovation \(ca.gov\)](http://Licenses and Industries Regulated by the Department | The Department of Financial Protection and Innovation (ca.gov))
- In New York, the Department of Financial Services licenses foreign banks: [Who We Supervise | Department of Financial Services \(ny.gov\)](http://Who We Supervise | Department of Financial Services (ny.gov))

Does the financial institution qualify as a depository institution?

- If the entity accepts retail deposits and is FDIC insured, it qualifies as a depository institution as determined by the FDIC and Federal Reserve System. If the entity does not accept retail deposits, seek legal advice to determine whether the entity

qualifies as a depository institution. The National Information Center provides information whether an issuing entity is an “insured” or “uninsured” branch or agency. www.ffiec.gov/nicpubweb/nic-web/NicHome.aspx.

ESTABLISHING THE ELIGIBILITY OF FOREIGN AND FOREIGN AFFILIATED ISSUERS OF PERMISSIBLE INVESTMENTS

Medium-Term Notes – G.C. Section 53601(k)

Medium-term notes are debt instruments issued by corporations and depository institutions with maximum remaining maturities of 5 years or less.

In 1987, government code allowing corporate debt as a permissible investment was amended changing the language from “corporations operating within the United States” to “corporations organized and operating within the United States” to address concerns of the California Municipal Treasurers Association that investment in foreign corporations presented a risk because often no financial information was available.⁴

Section (k) contains “*organized*”, “*operating*”, and “*licensed*” as terms defining what is a permissible issuer: “[a]ll corporate and depository institution debt securities with a maximum remaining maturity of *five years or less*, issued by *corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.*”⁵

Local agencies should verify that the foreign affiliate entity qualifies as eligible using the resources identified under *Sources of Information on Affiliates of Foreign Corporations* and *Sources of Information on Federally- and State-licensed Foreign Banks and Affiliates* in the previous section.

Supranational Notes – G.C. Section 53601(q)

Section 53601(q) allows local agencies to invest in United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by one of three supranational organizations: International Bank for Reconstruction and Development, International Finance Corporation, and Inter-American Development Bank. Each of these entities was established by international treaties, incorporated into U.S. federal law by Congressional acts and headquartered in Washington, D.C. Currently, these entities carry the highest credit ratings (AAA) based on their financial structure, policies, performance and capital support from shareholders.⁶

Section 53601(q) does not contain the terms “*organized*”, “*operating*”, or “*licensed*”, but does reference the eligible quasi-foreign entities (supranational organizations) by name.

Commercial Paper – G.C. Section 53601(h)

Commercial paper is an unsecured, short-term promissory note with a maximum maturity of 270 days or less issued by corporations, special purpose corporations, trusts, or limited liability companies.

Section 53601(h) references eligible issuers as entities that are “*organized*” and “*operating*” in the United States as a general corporation, or “*organized*” within the United States as a special purpose corporation, trust, or limited liability company. There is no qualifying criterion to be “*licensed*” within the section. Local agencies should verify the foreign affiliated entity’s status as “*organized*” or “*operating*” in the United States before investing. Refer to *Sources of Information on Affiliates of Foreign Corporations* in the previous section.

⁴ Office of Local Government Affairs, *Enrolled Bill Report Senate Bill (SB) 962* (As Amended 5/19/87), Session 1987-1988, Author: Bergeson, Subject: Funds of Local Agencies

⁵ Emphasis added

⁶ *Local Agency Investment Guidelines, Update for 2025*, p. 21

Negotiable Certificates of Deposit - G.C. Section 53601 (i)

Negotiable certificates of deposit (NCDs) are typically short-term debt instruments that pay interest periodically and pay principal at maturity. The majority of NCDs mature within six months to a year although some may have longer maturities.⁷ The term “negotiable” means there is an active secondary market where NCDs can be purchased or sold at any time between the issue date and the maturity date.

In 2011, legislation was enacted adding NCDs issued by federally licensed “Yankee Banks” as permitted investments. At the time, the California Association of County Treasurers and Tax Collectors noted that changes in banking regulations had resulted in the establishment of federally chartered branches of foreign banks (Yankee Banks), but that state law didn’t recognize those institutions’ certificates of deposit. This legislation added federally licensed or state licensed branches of foreign banks to the list of financial institutions whose certificates of deposit are eligible for local agencies’ investments.⁸

Currently the section contains the term “*licensed*”, specifically “a federally licensed or state-licensed branch of a foreign bank” and are subject to the limitations of section 53638 regarding the deposit of funds. Local agencies should verify that the bank is a federally licensed or state-licensed branch of a foreign bank using the *Sources of Information on Federally- and*

State-licensed Foreign Banks and Affiliates in the previous section.

Bankers' Acceptances – G.C. Section 53601(g)

Bankers’ acceptances (BAs) are money market instruments created when a bank accepts responsibility from a borrower for future payment of a bank draft or letter of credit in a financing transaction then sells the obligation to investors. BAs are issued by foreign and U.S. banks, sold at a discount and mature at par generally within six months or less of issuance. The bank guarantees payment of the BA at maturity.⁹

Section 53601(g) does not specifically describe a foreign bank as a qualifying issuing entity using terms such as “*organized*”, “*operating*”, and “*licensed*” as they are used in the subsections for commercial paper and negotiated certificates of deposit. Due to this gray area, CDIAC recommends that local agencies verify that foreign banks are either federally licensed or state-licensed using the *Sources of Information on Federally- and State-licensed Foreign Banks and Affiliates* in the previous section.

SUMMARY

Prior to purchasing the notes, certificates, and obligations of the affiliates of foreign firms pursuant to Government Code sections 53601(k), (q), (g), (h), (i), local agencies must determine whether the instruments as well as the issuing entities meet specific qualifying criteria.

Although the maturity, credit rating, and portfolio allocation requirements are straightforward, the legal and regulatory complexities inherent in the incorporation and licensing status of foreign affiliated issuers can present challenges to making a clear determination of the statutory permissibility of an investment, and at times, may need a more thorough legal analysis. Local agencies, in consultation with their legal counsel, should establish a procedure for determining whether the issuing entity meets the requirements of the specific subsection of section 53601 before purchasing securities from these entities. In addition, local agency investment staff should evaluate the risks and benefits of instruments issued by foreign affiliated entities with unclear incorporation or licensing status with those that clearly meet the requirements of section 53601.

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⁷ California Public Fund Investment Primer, CDIAC 09-02, p. 68, www.treasurer.ca.gov/cdiac/invest/primer.pdf, accessed July 2024, p. 68

⁸ *Senate Floor Analyses, Senate Rules Committee, SB 194 (amended on 06/13/2011)*, Session 2011-2012, Author: Senate Governance and Finance Committee, https://leginfo.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201120120SB194#, accessed July 2024, p. 5.

⁹ California Public Fund Investment Primer, p. 60

Appendix A: Statutory Requirements for Investments in the Debt of Foreign and Foreign Affiliated Issuers

INVESTMENT TYPE	STATUTORY REQUIREMENTS FOR FOREIGN-ISSUED DEBT TO BE A PERMISSIBLE INVESTMENT
<p>MEDIUM TERM NOTES Gov't Code section: 53601 (k)</p>	<ul style="list-style-type: none"> • Maximum remaining maturity of five years or less • In a rating category of "A" or its equivalent or better by a nationally recognized statistical rating origination (NRSRO) • Cannot exceed 30% of the agency's investment portfolio • Not including counties or a city and county, no more than 10% of an agency's total investment assets in the commercial paper and the medium-term notes of any single issuer • Foreign affiliated issuers shall be corporations organized and operating in the United States, or the foreign affiliated issuers are depository institutions licensed by the United States or any state and operating within the United States
<p>SUPRANATIONAL OBLIGATIONS Gov't Code section: 53601 (q)</p>	<ul style="list-style-type: none"> • Maximum remaining maturity of five years or less • United States dollar denominated senior unsecured unsubordinated obligations, eligible for purchase and sale in the U.S. • Issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank • In a rating category of "AA" or its equivalent or better by a nationally recognized statistical rating organization (NRSRO) • Cannot exceed 30% of the agency's investment portfolio
<p>NEGOTIABLE CERTIFICATES OF DEPOSIT Gov't Code section: 53601 (i)</p>	<ul style="list-style-type: none"> • Maximum remaining maturity of five years or less • Cannot exceed 30% of the agency's investment portfolio • Foreign bank issuers must be state or federally licensed branches
<p>COMMERCIAL PAPER Gov't Code sections: 53601 (H)(2)(C), 53635</p>	<ul style="list-style-type: none"> • Maturity 270 days or less • In a rating category of "prime" quality of the highest ranking or of the highest letter and number rating as provided for by a nationally recognized statistical rating organization (NRSRO) • Foreign affiliated issuers shall be corporations organized and operating in the United States, with total assets in excess of \$500,000,000 and other non-commercial paper debt rated in the category of "A" or higher • Alternatively, foreign affiliated issuers shall be organized in the U.S. as a special purpose corporation, trust, or limited liability company, have credit enhancements in place for their commercial paper program, and have commercial paper that is rated "A-1" or the equivalent, or higher • Portfolio limitations: <i>Agencies not counties, a city and county, the city of Los Angeles, or local agency pools</i> <ul style="list-style-type: none"> • Cannot exceed 25% of the agency's investment portfolio for local agencies that have less than \$100,000,000 of investment assets under management • Cannot exceed 40% of the agency's investment portfolio for local agencies that have \$100,000,000 or more of investment assets under management • May invest no more than 10% of the agency's investment portfolio in the commercial paper and medium-term notes of any single issuer • <i>Counties, a city and county, the city of Los Angeles, or local agency pools</i> <ul style="list-style-type: none"> • May invest no more than 40% of the agency's money in eligible commercial paper • May invest no more than 10% of the total investment assets of the local agency in any one issuer's commercial paper
<p>BANKER'S ACCEPTANCES Gov't Code section: 53601 (g)</p>	<ul style="list-style-type: none"> • Maturity 180 days or less • Cannot exceed 40% of the agency's investment portfolio • No more than 30% of the agency's money may be invested in bankers' acceptances of any one commercial bank