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Loans to One Borrower Limitations Interim Compliance Provision

RESCINDED

Summary: This Bulletin provides interim guidance to savings association management on the general limitations and loan renewal aspects of the loans to one borrower limitations contained in the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA).

For Further Information Contact: Your District Office or the Thrift Programs Division of the Office of Thrift Supervision, Washington, D.C.

Thrift Bulletin 32-1

Background

There has been unavoidable confusion since the enactment of FIRREA concerning how a savings association should apply the loans to one borrower limitations contained in the legislation. The legislation states that Section 5200 of the Revised Statutes (12 U.S.C. Section 84) is to "apply to savings associations in the same manner and to the same extent as it applies to national banks." FIRREA also provides the Director of the Office of Thrift Supervision (OTS) with authority to impose more stringent loans to one borrower restrictions.

General Limitations

Savings associations' management shall apply the Office of the Comptroller of the Currency's (OCC) lending limit regulations and codified opinions, which are promulgated pursuant to notice and comment and are binding on associations. Associations' management are also advised to apply the prior limitation at 12 C.F.R. Section 563.9-3, to the extent it is more restrictive, until the OTS issues its revised loans to one borrower regulations; however, with respect to the renewal of any loan that was legal when made, such loan may be renewed in accordance with the OCC's loan renewal policy as described herein. Although the OTS will give the Comptroller's legal opinions (noncodified) substantial weight, these opinions will not be regarded as legally binding on savings associations. Management should document that, in good faith, the more conservative lending limit has been applied in granting loans and extensions of credit. Management should further consult with their association's legal counsel for assistance in determining their appropriate lending limitations. Generally, the OTS will not take any supervisory action if the savings association's documentation demonstrates that it has taken the most conservative position during the time period from passage of FIRREA until the new OTS regulations are effective.

Particular Guidance with Respect to Loan Renewals

A renewal of a loan is generally not regarded as the equivalent of a new loan at the time of renewal for lending limit purposes, provided: (1) no new funds are advanced by the association to the borrower; and (2) a new borrower is not substituted for the original obligor. A loan restructuring, to include extended repayment terms, altered interest rates, or the taking of additional security, will be treated as a loan renewal rather than a new loan and extension of credit, provided that the original obligor on the loan is not released (other obligors may be added).

Funded portions of commitments may similarly be renewed; however, unfunded portions may not. For example, if an association has a $10,000,000 commitment to a borrower which was within the legal lending limit when made, with $6,000,000 funded at the date that the commitment expires, the association could renew up to $6,000,000 as if the commitment were a term loan, even though the association's legal lending limit is now less than $6,000,000.

Provided conditions (1) and (2) stated above are met, the renewal of such loans will not result in a violation of the new statutory limitation; rather, the loans will be deemed "nonconforming." The use of this term is consistent with the OCC's usage, and such loans are not the same as nonconforming loans as defined in Section 5(c)(3)(C) of the Home Owners' Loan Act of 1933.

Because the renewal of a nonconforming loan presents an opportunity to bring the loan into conformance, however, the association must prior to such a renewal make every effort to bring the loan into conformance with the new limitation. For example, the association should attempt to have the debtor partially repay the loan or obtain

another institution's nonparticipation in the loan to bring it into lending limit compliance is incumbent upon the association to demonstrate with written evidence that such efforts have been made. Such evidence should be presented to the appropriate person, committee, or the board of directors in conjunction with the loan approval process.

The OTS will not consider the renewal made in accordance with these principles to be a violation of law. Circumstances that indicate a deliberate purpose to evade the law and to extend unwarranted lines of credit would violate the statutory limitations made applicable by FIRREA and expose the directorate to liability. Furthermore, efforts to bring a loan into conformance do not end with the loan's renewal. Management should continue to document its efforts to bring such nonconforming loans into conformance on an ongoing basis.

This position is consistent with the longstanding policy of the OCC as expressed in their written interpretations of applicable statutory and case law.

The appendix to this Bulletin includes pertinent sections of the Comptroller's regulations as guidance for determining an association's unimpaired capital and unimpaired surplus upon which the loans to one borrower limitations shall currently be based.

Attachment

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PART 1—INVESTMENT SECURITIES REGULATION

Sec.
1.1 Authority.
1.2 Scope and application.
1.3 Definitions.
1.4 Type I securities; standards for authorized transactions.
1.5 Types II and III securities; purchase standards.
1.6 Type II securities; authority to deal in and underwrite.
1.7 Types II and III securities; limitations on holdings.
1.8 Prudent banking judgment; credit information required.
1.9 Requests for rulings.
1.10 Convertible securities.
1.11 Amortization of premiums.
1.12 Exceptions.
1.100 Eligibility of securities for purchase, dealing in, and underwriting by national banks; general guidelines.
1.110 Obligations of the United States; general guidelines.
1.120 Indirect general obligations; general guidelines.
1.130 Taxing powers of a State or a political subdivision thereof; general guidelines.
1.140 Type II securities; general guidelines.

AUTHORITY: R.S. 324, et seq., as amended (12 U.S.C. 1, et seq.); Paragraph Seventh of R.S. 5136, as amended (12 U.S.C. 24(7)).

§ 1.1 Authority.

This part is issued by the Comptroller of the Currency under the general authority of the national banking laws, 12 U.S.C. 1 et seq., and under specific authority contained in paragraph Seventh of 12 U.S.C. 24. The Comptroller of the Currency is charged by the national banking laws with the execution of all laws of the United States relating to the organization, operation, regulation and supervision of national banks and in particular with the execution of 12 U.S.C. 24 which sets forth the corporate powers of national banks. This part interprets and applies paragraph Seventh of 12 U.S.C. 24 to provide for its due execution and for the proper regulation and supervision of the operations of national banks. Paragraph Seventh of 12 U.S.C. 24 also specifically provides for the Comptroller of the Currency to prescribe by regulation (a) limitations and restrictions on the purchase of investment securities by a national bank for its own account and (b) further definition of the term "investment securities."

[28 FR 9016, Sept. 12, 1963]

§ 1.2 Scope and application.

This part applies to the purchase, sale, dealing in, underwriting, and holding of investment securities by national banks, banks located in the District of Columbia, and by state banks which are members of the Federal Reserve System. It may also apply to a limited extent to others engaged in the banking business. The Comptroller of the Currency is charged by various provisions contained in Chapter 1 of Title 26 of the District of Columbia Code with the supervision of banks located in the District of Columbia. State banks which are members of the Federal Reserve System are, under 12 U.S.C. 335, subject to the same limitations and conditions with respect to the purchasing, selling, underwriting, and holding of investment securities and stock as are applicable in the case of national banks under paragraph Seventh of 12 U.S.C. 24. Dealers in securities are prohibited by 12 U.S.C. 378 from engaging in banking business. Section 378 specifically provides, however, that it does not prohibit national banks or state banks or trust companies (whether or not members of the Federal Reserve System) or other financial institutions or private bankers from dealing in, underwriting, purchasing and selling investment securities to the extent permitted to national banking associations by the provisions of 12 U.S.C. 24.

[28 FR 9016, Sept. 12, 1963]

§ 1.3 Definitions.

(a) The term "bank" includes national banks, banks located in the District of Columbia, and State banks which are members of the Federal Reserve System.

(b) The term "investment security" means a marketable obligation in the form of a bond, note, or debenture which is commonly regarded as an investment security. It does not include investments which are predominantly speculative in nature.

(c) The term "Type I security" means a security which a bank may deal in, underwrite, purchase and sell for its own account without limitation. These include obligations of the United States, general obligations of any State of the United States or any political subdivision thereof and other obligations listed in paragraph Seventh of 12 U.S.C. 24.

(d) The term "Type II security" means a security which a bank may deal in, underwrite, purchase, and sell for its own account, subject to a 10-percent limitation. These include obligations of the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank and the Tennessee Valley Authority, and obligations issued by any State or political subdivision or any agency of a State or a political subdivision for housing, university or dormitory purposes.

(e) The term "Type III security" means a security which a bank may purchase and sell for its own account, subject to a 10-percent limitation, but may neither deal in nor underwrite.

(f) The term "political subdivision of any State" includes a county, city, town, or other municipal corporation, a public authority, and generally any publicly owned entity which is an instrumentality of the State or of a municipal corporation.

(g) The phrase "general obligation of any State or any political subdivision thereof" means an obligation supported by the full faith and credit of an obligor possessing general powers of taxation, including property taxation. It includes an obligation payable from a special fund or by an obligor not possessing general powers of taxation when an obligor possessing general powers of taxation, including property taxation, has unconditionally promised to make payments into the fund or otherwise available for the payment of the obligation of amounts which (together with any other funds available for the purpose) will be sufficient to provide for all required payments in connection with the obligation.

[36 FR 6737, Apr. 8, 1971]

§ 1.4 Type I securities; standards for authorized transactions.

Type I securities are not subject to the limitations and restrictions contained in 12 U.S.C. 24 or in this Part other than §§ 1.3(c), 1.3(g), 1.4, 1.8, 1.9, and 1.11. Consequently, a bank may deal in, underwrite, purchase, and sell for its own account a security of Type I subject only to the exercise of prudent banking judgment. Prudence will require such determinations as are appropriate for the type of transaction involved. For the purpose of underwriting or investment, prudence will also require a consideration of the resources and obligations of the obligor and a determination that the obligor possesses resources sufficient to provide for all required payments in connection with the obligations.

[36 FR 6737, Apr. 8, 1971]

PART 3—MINIMUM CAPITAL RATIOS; ISSUANCE OF DIRECTIVES

Subpart A—Authority and Definitions

Subpart B—Minimum Capital Ratios

Subpart C—Establishment of Minimum Capital Ratios for an Individual Bank

Subpart D—Enforcement

AUTHORITY: 12 U.S.C. 1 *et seq.*; 12 U.S.C 93a, 161, 1818; and 12 U.S.C. 3907 and 3909.

SOURCE: 50 FR 10216, Mar. 14, 1985, unless otherwise noted.

Subpart A—Authority and Definitions

§ 3.1 Authority.

This part is issued under the authority of 12 U.S.C. 1 *et seq.*, 93a, 161, 1818; and the International Lending Supervision Act of 1983 (Pub. L. 98-181, Title IX, 97 Stat. 1153), 12 U.S.C. 3907 and 3909.

§ 3.2 Definitions.

For the purposes of this part:

(a) "Adjusted total assets" means the average total assets figure required to be computed for and stated in a bank's most recent quarterly "Consolidated Report of Condition and Income" (Call Report), plus the end-of-quarter allowance for loan and lease losses, minus end-of-quarter intangible assets not included in primary capital. The Office reserves the right to require a bank to compute and maintain its capital ratios on the basis of actual, rather than average, total assets when necessary to carry out the purposes of this regulation.

(b) "Bank" means a national banking association or a District of Columbia bank.

(c) "Primary capital" means the sum of paragraphs (c) (1), (2) and (3) of this section.

(1) Common stock, perpetual preferred stock, capital surplus, undivided profits, reserves for contingencies and other capital reserves (excluding accrued dividends on perpetual and limited life preferred stock), net worth certificates issued pursuant to 12 U.S.C. 1823

(i) Minority interests in consolidated subsidiaries, and allowances for loan and lease losses; minus intangible assets;

(2) Purchased mortgage servicing rights; and

(3) Mandatory convertible debt to the extent of 20% of the sum of paragraphs (c) (1) and (2) of this section.

(d) "Secondary capital" means the sum of paragraphs (d) (1) and (2) of this section, to the extent that this figure does not exceed 50% of the bank's primary capital: (1) Mandatory convertible debt that is not included in primary capital; and (2) limited life preferred stock and subordinated notes and debentures. These instruments must meet the requirements set forth in 12 CFR 3.100 or otherwise published by the Office (A bank may issue mandatory convertible debt, other subordinated debt or limited life preferred stock in amounts exceeding the limitation in this paragraph, but such stock or debt shall not be considered capital for capital adequacy or statutory purposes without the written approval of the Office.).

(e) "Total capital" means the sum of primary capital and secondary capital. The end-of-quarter figures as of the Call Report date shall be used in computing the bank's capital ratios.

INTERPRETATIONS

§ 3.100 Capital and surplus.

(a) *Capital.* The term "capital" as used in provisions of law relating to the capital of national banking associations shall include the amount of common stock outstanding and unimpaired plus the amount of perpetual preferred stock outstanding and unimpaired.

(b) *Capital Stock.* The term "capital stock" as used in provisions of law relating to the capital stock of national banking associations, other than 12 U.S.C. 101, 177 and 178, shall have the same meaning as the term "capital" set forth in paragraph (a) of this section.

(c) *Surplus.* The term "surplus" as used in provisions of law relating to the surplus of national banking associations means the sum of paragraphs (c) (1), (2), (3) and (4) of this section:

(1) Capital surplus; undivided profits; reserves for contingencies and other capital reserves (excluding accrued dividends on perpetual and limited life preferred stock); net worth certificates issued pursuant to 12 U.S.C. 1823(i); minority interests in consolidated subsidiaries; and allowances for loan and lease losses; minus intangible assets;

(2) Purchased mortgage servicing rights;

(3) Mandatory convertible debt to the extent of 20% of the sum of paragraphs (a) and (c) (1) and (2) of this section;

(4) Other mandatory convertible debt, limited life preferred stock and subordinated notes and debentures to the extent set forth in paragraph (f)(2) of this section.

(d) *Unimpaired Surplus Fund.* The term "unimpaired surplus fund" as used in provisions of law relating to the unimpaired surplus fund of national banking associations shall have the same meaning as the term "surplus" set forth in paragraph (c) of this section.

(e) *Definitions.* (1) "Allowance for loan and lease losses" means the balance of the valuation reserve on December 31, 1968, plus additions to the reserve charged to operations since that date, less losses charged against the allowance net of recoveries.

(2) "Capital surplus" means the total of those accounts reflecting:

(i) Amounts paid in in excess of the par or stated value of capital stock;

(ii) Amounts contributed to the bank other than for capital stock;

(iii) amounts transferred from undivided profits pursuant to 12 U.S.C. 60; and

(iv) Other amounts transferred from undivided profits.

(3) "Intangible assets" means those purchased assets that are to be reported as intangible assets in accordance with the "Instructions—Consolidated Reports of Condition and Income" (Call Report).

(4) "Limited Life preferred stock" means preferred stock which has a maturity or which may be redeemed at the option of the holder.

(5) "Mandatory convertible debt" means subordinated debt instruments which unqualifiedly require the issuer to exchange either common or perpetual preferred stock for such instruments by a date at or before the maturity of the instrument. The maturity of these instruments must be 12 years or less. In addition, the instrument must meet requirements of paragraphs (e)(2)(i) through (v) of this section for subordinated notes and debentures contained in paragraph (f)(1) of this section or other requirements published by the Office.

(6) "Minority interest in consolidated subsidiaries" means the portion of equity capital accounts of all consolidated subsidiaries of the bank that is allocated to minority shareholders of such subsidiaries.

(7) "Mortgage servicing rights" means the bank-owned rights to service for a fee mortgage loans that are owned by others.

(8) "Perpetual preferred stock" means preferred stock that does not have a stated maturity date and cannot be redeemed at the option of the holder.

(f) *Requirements and Restrictions: Limited Life Preferred Stock, Mandatory Convertible Debt, and Other Subordinated Debt*—(1) *Requirements.* Issues of limited life preferred stock and subordinated notes and debentures (except mandatory convertible debt) must have original weighted average maturities of at least seven (7) years to be included in the definition of "surplus." In addition, a subordinated note or debenture must also:

(i) Be subordinated to the claims of depositors;

(ii) State on the instrument that it is not a deposit and is not insured by the FDIC;

(iii) Be approved as capital by this Office;

(iv) Be unsecured;

(v) Be ineligible as collateral for a loan by the issuing bank;

(vi) Provide that once any scheduled payments of principal begin, all scheduled payments shall be made at least annually and the amount repaid in each year shall be no less than in the prior year; and

(vii) Provide that no accelerated payment by reason of default or otherwise may be made without the prior written approval of the Office.

(2) *Restrictions.* The total amount of mandatory convertible debt not included in paragraph (c)(3) of this section, limited life preferred stock, and subordinated notes and debentures considered as surplus is limited to 50 percent of the aggregate amount of primary capital, as defined in 12 CFR 3.2(c), unless specifically approved in writing by the Office.

(3) *Reservation of Authority.* The OCC expressly reserves the authority, in exigent circumstances, to waive the minimum maturity requirement and the percentage restriction set forth in paragraphs (f) (1) and (2) of this section, in order to allow the inclusion of other limited life preferred stock, mandatory convertible notes and subordinated notes and debentures in the capital base of any national bank for capital adequacy purposes. The OCC further expressly reserves the authority in exigent circumstances, to impose more stringent conditions than those set forth in paragraphs (f) (1) and (2) of this section in order for any component of primary or secondary capital to be included, in whole or in part, as part of a national banking association's capital and surplus for any purpose.

(Approved by the Office of Management and Budget under control number 1557-0166)