

## OFFICE OF THRIFT SUPERVISION

### Order Approving an Application To Establish a Service Corporation

**Order No.:** 2009-19  
**Date:** April 8, 2009  
**Docket No.:** 16456

Bank of Internet, USA, San Diego, California (Savings Bank), a Federal savings bank, has filed an application with the Office of Thrift Supervision (OTS) under 12 U.S.C. § 1828(m) and 12 C.F.R. Part 559, requesting approval to establish a service corporation, BofI Structured Settlement Funding Corporation, San Diego, California (Service Corporation) to engage in activities related to structured settlement arrangements. The Savings Bank would establish the Service Corporation as its wholly owned subsidiary.

#### **The Proposed Transaction**

The Savings Bank will organize the Service Corporation as a California-chartered corporation and will hold all of the Service Corporation's outstanding common stock. The Service Corporation will engage in structured settlement arrangements. A structured settlement arrangement typically is an arrangement by a person (Beneficiary) who has been granted an award or benefit under which another party (Paying Party) agrees to pay the Beneficiary a regular periodic payment for the life of the Beneficiary or for a fixed number of years. These settlement arrangements are usually effected by having the Paying Party acquire an annuity from an insurance company, which is payable to the Beneficiary. In some cases, the Beneficiary may prefer a lump sum payment immediately rather than a periodic payment over an extended period of time. In such a case, a third party may acquire from the Beneficiary the right to the periodic payments in exchange for a current payment to the Beneficiary. Such an arrangement in the context of a structured settlement in California must be approved in a court proceeding, generally by the same judge that approved the original settlement agreement. The Service Corporation would be the third party advancing funds to the Beneficiary and receiving repayment from a specific source, the insurance company.

#### **Service Corporation Application**

In considering whether a proposed investment in a service corporation by a federal savings association is permissible, OTS must consider whether the activity is permissible, whether the amount of the investment is permissible, the state of incorporation of the proposed service corporation and the nature of the investors, and whether there are any supervisory or safety and soundness reasons to limit or to refuse to permit the investment.

Permissible Service Corporation Activities

Section 5(c)(4)(B) of the Home Owners' Loan Act (HOLA), which authorizes Federal savings associations to invest in service corporations, does not specify the types of activities in which service corporations may engage. Section 559.3(e)(2) of the OTS Subordinate Organization Regulation provides that a Federal association may request approval for a service corporation to engage in any activity that is reasonably related to the activities of financial institutions.<sup>1</sup> There are no specific criteria for determining whether an activity meets the "reasonably related" standard. However, in certain previous cases OTS has considered whether the purpose of the activity and the types of risks it presents are similar to the purpose and risks of other activities conducted by Federal savings associations.<sup>2</sup>

Federal savings associations are authorized to make loans for, among other things, personal, family and household purposes.<sup>3</sup> A structured settlement is similar to a loan because the Service Corporation will advance funds to the Beneficiary for the Beneficiary's personal, family and household purposes.

Structured settlement arrangements are also a means of providing liquidity to the recipient, *i.e.*, the Beneficiary, of the funds. Federal savings associations provide liquidity in other types of transactions, *e.g.*, in lending transactions and as a factor. The Service Corporation will provide a certain amount of funds currently to the Beneficiary against the Beneficiary's dedicated future periodic cash flows from a specific source.

With respect to risk, in a structured settlement arrangement, repayment proceeds are derived from a specific asset, typically, an insurance or annuity policy, in contrast to a typical loan repayment wherein the borrower is expected to repay the loan from any sources available to the borrower. OTS notes, however, that structured settlement arrangements are similar in many respects to reverse mortgages,<sup>4</sup> which have been offered by Federal associations for several years. In the reverse mortgage, the lender does not rely on periodic payments from the borrower, but relies on one or more assets of the borrower (normally, the borrower's residence). In both cases, the risk presented is not credit risk, but the financial institution's ability to evaluate the time value of money in relation to the value of an underlying asset. In structured settlement arrangements, the Service Corporation intends to mitigate payment risk by entering into arrangements principally with highly rated insurance companies. Further, the Service Corporation intends to mitigate risk by entering only into arrangements under which a

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<sup>1</sup> Structured settlement arrangements are not a preapproved activity for a service corporation under section 559.4.

<sup>2</sup> BTD Opinion, Aug. 3, 2005; BTD Opinion, May 7, 1997.

<sup>3</sup> 12 U.S.C. § 1464(c)(2)(D).

<sup>4</sup> Typically, a reverse mortgage enables an elderly homeowner, who has paid off his mortgage, to borrow against the equity in his property. The credit may be in the form of a lump sum, a line of credit, or series of monthly payments to the customer.

Beneficiary is entitled to payments for a stated period, rather than those with a period tied to the Beneficiary's lifetime.

Structured settlement arrangements are similar to viatical arrangements, which OTS has previously approved as a service corporation activity after undertaking a similar analysis.<sup>5</sup> Viatical financing involves the acquisition, at a discount, of insurance policies from persons suffering terminal illnesses. Such an acquisition of an insurance policy by a viatical company enables the owner to obtain a portion of the face amount of the policy immediately. Upon the policyholder's demise, the viatical company collects the face amount of the policy. In the case of viatical financing, like structured settlements, the financial intermediary provides funds to a beneficiary for personal, family and household purposes, and relies on a specific asset for repayment. While the risk in the proposed structured settlements relates to the ability of the insurance company to perform on its obligation, in viatical financing, the risks relate both to the insurance company's performance, and to the lifespan of the insured.

Based on the foregoing analysis, OTS concludes that the purposes and risks presented by the proposed activity are similar to the risks presented by the lending operations of a Federal savings association. Accordingly, OTS concludes that the Service Corporation's proposed structured settlement activities are reasonably related to the activities of a financial institution.

#### Other Approval Criteria

Section 5(c)(4)(B) of the HOLA authorizes "[i]nvestments in the capital stock, obligations, or other securities of any corporation organized under the laws of the State in which the Federal savings association's home office is located . . . ." The Savings Bank's home office is located in California. The Service Corporation is a California corporation. Accordingly, the application is consistent with this requirement.

Section 5(c)(4)(B) also requires that only savings associations with home offices in the Savings Bank's home state may have an ownership interest in a first-tier service corporation. The Savings Bank will own all of the stock of the proposed service corporation. Accordingly, the application meets this requirement.

Based on the Savings Bank's total assets of approximately \$1.22 billion as of December 31, 2008, the amount of permissible service corporation investments (not including investments that serve primarily community, inner city, or community development purposes) is two percent of assets, or approximately \$24.38 million. The projected investment in the new service corporation is approximately \$24.05 million and will be the Savings Bank's only service corporation investment. This level of investment is within the two percent limitation on service corporation investments of this type, under section 5(c)(4)(B) of the HOLA and 12 C.F.R. § 559.5(a).

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<sup>5</sup> OTS Order No. 97-49, May 20, 1997.

OTS concludes that the application presents sufficient information to conclude that the service corporation will comply with the separate corporate identity requirements of 12 C.F.R. § 559.10. OTS is imposing condition 6 to help ensure the safe and sound operations of the Savings Bank and the Service Corporation.

### **Conclusion**

For the reasons set forth above, OTS concludes that the service corporation application satisfies the applicable approval standards, provided that the following conditions are complied with in a manner satisfactory to the West Regional Director, or his designee (Regional Director). Accordingly, the application is hereby approved, subject to the following conditions:

1. The Savings Bank and Service Corporation must receive all required regulatory approvals prior to completing the transaction with copies of the approvals provided to the Regional Director;
2. The Savings Bank must commence the proposed transaction no later than 120 days from the date of this Order;
3. On the business day prior to the date of consummation of the proposed transaction, the chief financial officer of the Savings Bank must certify in writing to the Regional Director that no material adverse changes have occurred with respect to the financial condition or operation of the Savings Bank as disclosed in the application. If additional information having a material adverse bearing on any feature of the application is brought to the attention of the Savings Bank or OTS since the date of the financial information submitted with the application, the transaction must not be consummated unless the information is presented to the Regional Director, and the Regional Director provides written non-objection to consummation of the transaction;
4. No later than five calendar days from the date of consummation of the transaction, the Savings Bank must file with the Regional Director a certification by legal counsel stating the effective date of the transactions, and that the transaction has been consummated in accordance with the provisions of all applicable laws and regulations, the application, and this Order;
5. The Service Corporation must not deviate materially from any of the activities, facts or representations described in the application, except with the prior written non-objection of the Regional Director, or his designee; and
6. The Savings Bank must submit to the Regional Director for his written non-objection, within 30 days of the date of the approval of the application, a copy of

the Service Corporation's board-approved comprehensive policies and procedures governing the structured settlement activity including, but not limited to, the performance of due diligence on the issuing insurance company, consumer protection, activity risk management, and tracking and monitoring controls.

The Regional Director may, for good cause, extend any time period specified herein for up to 120 calendar days.

By Order of the Acting Director of the Office of Thrift Supervision, or his designee, effective 4/8/2009.



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Grovetta N. Gardineer  
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Corporate & International Activities