



FEDERAL RESERVE BANK
OF DALLAS

ROBERT D. McTEER, JR.
PRESIDENT
AND CHIEF EXECUTIVE OFFICER

June 1, 1993

DALLAS, TEXAS 75222

Notice 93-59

TO: The Chief Executive Officer of each member bank and others concerned in the Eleventh Federal Reserve District

SUBJECT

Final Rule Amending Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks)

DETAILS

The Federal Reserve Board has amended Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks) to implement recent amendments to section 22(h) of the Federal Reserve Act, contained in the Housing and Community Development Act of 1992.

The final rule adopts three exceptions to the aggregate insider lending limit in Regulation O substantially as they were set forth in the Board's proposed rule. Additional exceptions suggested by commenters will be considered in future rulemaking.

ATTACHMENT

A copy of the Board's notice (Federal Reserve System Docket No. R-0785) is attached.

MORE INFORMATION

For more information, please contact Jane Anne Schmoker at (214) 922-5104. For additional copies of this Bank's notice, please contact the Public Affairs Department at (214) 922-5254.

Sincerely yours,

Robert D. McTeer, Jr.

FEDERAL RESERVE SYSTEM

12 CFR Part 215

[Regulation O; Docket No. R-0785]

Loans to Executive Officers, Directors, and Principal
Shareholders of Member Banks; Loans to Holding Companies and
Affiliates

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board is amending Regulation O to implement recent amendments to section 22(h) of the Federal Reserve Act, contained in the Housing and Community Development Act of 1992. The final rule adopts three exceptions to the aggregate insider lending limit in Regulation O substantially as they were set forth in the Board's proposed rule. Additional exceptions suggested by commenters will be considered in future rulemaking.

EFFECTIVE DATE: May 3, 1993.

FOR FURTHER INFORMATION CONTACT: Gordon Miller, Attorney (202/452-2534), Legal Division, Board of Governors of the Federal Reserve System. For the hearing impaired only, Telecommunication Device for the Deaf (TDD), Dorothea Thompson (202/452-3544), Board of Governors of the Federal Reserve System, 20th & C Streets, NW., Washington, DC 20551.

SUPPLEMENTARY INFORMATION:Background

The Housing and Community Development Act of 1992 (HCDA), Pub. L. 102-550, 106 Stat. 3672 (1992), effective October 28, 1992, amended section 22(h) of the Federal Reserve Act (Act), 12 U.S.C. 375(b), to authorize the Board to adopt exceptions from the definition of "extension of credit" that pose minimal risk to the lending bank. The legislative history of this provision states that the Board should make a "zero-based review" of all exceptions. See 138 Cong. Rec. S17,914-15 (daily ed. October 8, 1992). The Board has proposed three exceptions to the aggregate lending limit in Regulation O (12 CFR Part 215) to implement this amendment.

All of the proposed exceptions are found in the National Bank Act and are already incorporated in the individual lending limit in Regulation O. See 12 U.S.C. § 84; 12 CFR 215.2(h) and 215.4(c). These exceptions are for certain categories of loans or extensions of credit that are deemed, as a result of the manner in which they are collateralized, to pose minimal risk of loss to a bank. The proposed exceptions are in the following three categories:

- (1) Extensions of credit secured by obligations of the United States or other obligations fully guaranteed as to principal and interest by the United States;

- (2) Extensions of credit to or secured by commitments or guarantees of a department or agency of the United States; and
- (3) Extensions of credit secured by a segregated deposit account with the lending bank.

Proposal as Adopted

The Board has determined to adopt the three proposed exceptions, with the modifications discussed below. The Board anticipates that the final rule will reduce the regulatory and recordkeeping burden on banks and increase the ability of banks to make loans and other extensions of credit that pose little or no risk to the bank.

Although loans secured in accordance with these exceptions are removed from a bank's aggregate lending limit, such loans remain subject to the general prohibitions in Regulation O on extensions of credit to insiders found at §§ 215.4(a) and (b), as a safeguard against abuse of these exceptions.

Comments

In response to its proposal, the Board received 40 comments: 15 by banks, 8 by state or national bankers' associations, 8 by bank holding companies, 6 by Federal Reserve banks, 2 from law firms, and 1 by a banker's bank. Thirty-four commenters favored the exceptions. Six commenters favored other or further exceptions, and did not comment on the proposed exceptions. There were no commenters that opposed the exceptions.

Among the 34 comments in favor of the exceptions, 27 expressed one or more reasons for their support. Twenty commenters noted that loans within these categories would pose minimal risk to the lending bank, 7 commenters favored the exceptions because they would improve the ability of member banks to retain qualified outside directors, and 5 commenters supported the exceptions because, by reducing the inconsistency between the aggregate lending limit and the individual lending limit, they would reduce the regulatory burden on member banks. Accordingly, the commenters felt that the proposal is in the public interest.

One commenter suggested clarifying the proposed exceptions by incorporating directly into Regulation O certain interpretations by the Comptroller of the Currency of the exceptions contained in the National Bank Act.^{1/} See 12 CFR 32.6(d), (e), and (f). This commenter suggested that the Board clarify that the amount of an extension of credit that is excepted from the aggregate lending limit is limited to an amount equal to: (1) the current fair market value of the United States obligations or other obligations fully guaranteed as to principal and interest by the United States securing the extension of credit; (2) the amount of the commitment or guarantee of a department or agency of the United States securing the extension of credit; or (3) the amount of the member bank's perfected

^{1/} All interpretations by the Comptroller of the exceptions contained in 12 U.S.C. § 84 are applicable to Regulation O to the extent that these exceptions are incorporated by reference into or otherwise adopted in Regulation O.

security interest in the segregated, earmarked deposit account securing the extension of credit. This commenter also suggested that the Board clarify that an extension of credit is eligible in full for an exception if the unpaid principal amount thereof is secured or guaranteed as described above, and that it is not required that accrued and unpaid interest on the extension of credit also be so covered.

The Board has determined that the suggested clarifications are consistent with the Comptroller's interpretations of 12 U.S.C. § 84, and incorporate appropriate safeguards against abuse of the proposed exceptions. The Board also has clarified, consistent with the Comptroller's interpretation of 12 U.S.C. § 84, that a member bank is required to obtain a perfected security interest in United States obligations or other obligations fully guaranteed as to principal and interest by the United States in order for this exception to be effective.

Twenty-one of the commenters proposed other or further exceptions. These comments presented a variety of proposals, including, among others, the adoption of one or more additional exceptions to the lending limits found in 12 U.S.C. § 84, the adoption of certain exceptions not found in 12 U.S.C. § 84, and the adoption of exemptions that would reduce or eliminate the additional regulatory restrictions imposed on extension of credit by a member bank to its executive officers.^{2/} These proposals

^{2/} These provisions appear in 12 CFR 215.5 of Regulation O, and have been adopted pursuant to section 22(g) of the Act,
(continued...)

will be considered by the Board in the near future. However, the Board has decided not to address these proposals at this time in order not to delay the adoption of a final rule concerning the 3 exceptions proposed by the Board.

Final Regulatory Flexibility Act Analysis

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. § 601 et seq.), the Board hereby certifies that the final rule will not have a significant adverse effect on a substantial number of small institutions. The final rule should relieve the regulatory burden on all member banks, regardless of size, and will increase the ability of small member banks to make loans and other extensions of credit that pose little or no risk of loss to them, and to attract and retain outside directors to whom such loans may be made in the same manner and to the same extent as they may be made to persons who are not insiders of the member bank.

List of Subjects in 12 CFR Part 215

Credit, Federal Reserve System, Penalties, Reporting and record keeping requirements.

For the reasons set forth in the preamble, the Board amends Title 12 of the Code of Federal Regulations, Part 215, Subpart A, as follows:

^{2/}(...continued)
12 U.S.C. § 375a. The subject matter of these comments is outside the scope of the current rulemaking, but will be considered in connection with future rulemaking by the Board concerning Regulation O.

PART 215--LOANS TO EXECUTIVE OFFICERS, DIRECTORS, AND PRINCIPAL SHAREHOLDERS OF MEMBER BANKS

1. The authority citation for part 215 is revised to read as follows:

Authority: 12 U.S.C. 248(i), 375a, 375b(7), 1817 (k)(3) and 1972(2)(F)(vi), Pub. L. 102-550, 106 Stat. 3895 (1992).

Subpart A--Loans by Members Banks to Their Executive Officers, Directors, and Principal Shareholders

2. Section 215.4 is amended by adding a new paragraph (d)(3) to read as follows:

§215.4 General prohibitions.

* * * * *

(d) * * *

(3) Exceptions. The general limit specified in paragraph (d)(1) of this section does not apply to the following:

(i) Extensions of credit secured by a perfected security interest in bonds, notes, certificates of indebtedness, or Treasury bills of the United States or in other such obligations fully guaranteed as to principal and interest by the United States;

(ii) Extensions of credit to or secured by unconditional takeout commitments or guarantees of any department, agency, bureau, board, commission or establishment of the United States or any corporation wholly owned directly or indirectly by the United States; or

(iii) Extensions of credit secured by a perfected security interest in a segregated deposit account in the lending bank.

(iv) The exceptions in this paragraph (d)(3) apply only to the amount of such extensions of credit that are secured in the manner described herein.

By order of the Board of Governors of the Federal Reserve System, April 27, 1993.

(signed)

William W. Wiles
Secretary of the Board