FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. **10554**
July 23, 1992]

SAFETY AND SOUNDNESS STANDARDS

Request for Comment, by September 14, on Requirements of Section 132 of FDICIA

To All Depository Institutions, and Others Concerned, in the Second Federal Reserve District:

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board has requested public comment on an interagency advance notice of proposed rulemaking under Section 132 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA).

Comments should be received by September 14, 1992.

Section 132 of FDICIA requires each of the Federal banking agencies to prescribe safety and soundness standards for the insured depository institutions or depository institution holding companies that it regulates. In particular, the agencies must prescribe operational and managerial standards, compensation standards, and asset quality, earnings and stock valuation standards.

The advance notice of proposed rulemaking seeks public suggestions on methods to meet the requirements of Section 132 and does not propose safety and soundness standards.

Comments received in response to the notice will be considered in developing a proposed rulemaking that would be issued at a later date in consultation with the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the Federal Deposit Insurance Corporation.

The four Federal banking agencies are required by FDICIA to promulgate final regulations implementing Section 132 by August 1, 1993.

Printed on the following pages is the text of the interagency notice, as published in the *Federal Register* of July 15. Comments thereon should be submitted by September 14, 1992, and sent to the appropriate agency, as indicated in the notice. Comments or questions on this matter may also be directed, at this Bank, to:

Name	Tel. No.
Fred C. Herriman, Jr., Manager Domestic Surveillance Staff	212-720-7962
Manuel J. Schnaidman, Manager Bank Analysis Department	212-720-6710
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E. GERALD CORRIGAN,
President.

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DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Chapter I

[Docket No. 92-11]

FEDERAL RESERVE SYSTEM

12 CFR Chapter II

[Docket No. R-0766]

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Chapter III

RIN 3064-AB13

DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

12 CFR Part 563

[Resolution No. 92-239]

RIN 1550-AA54

Standards for Safety and Soundness

AGENCIES: Office of the Comptroller of the Currency, Treasury; Board of Governors of the Federal Reserve System; Federal Deposit Insurance Corporation; and Office of Thrift Supervision, Treasury.

ACTION: Joint advance notice of proposed rulemaking.

SUMMARY: The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board of Governors), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS) (collectively "the agencies") solicit comments on all aspects of the safety and soundness standards required to be prescribed under section 132 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) in order to assist them in the development of a proposed rule.

DATES: Written comments must be received on or before September 14, 1992.

ADDRESSES: Commenters may respond to any or all of the agencies. All comments will be shared among the agencies.

OCC: Communications Division, 250 E Street SW., Washington, DC 20219, attention: Docket No. 92-11. Comments will be available for public inspection and photocopying at the same location on business days between 9 a.m. and 5 p.m.

Board of Governors: Comments, which should refer to Docket No. R-0766, may be mailed to Mr. William Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue NW., Washington, DC 20551. Comments addressed to Mr. Wiles may also be delivered to the Board's mail room between 8:45 a.m. and 5:15 p.m., and to the security control room outside of those hours. Both the mail room and control room are accessible from the courtyard entrance on 20th Street between Constitution Avenue and C Street, NW. Comments may be inspected in room B-1122 between 9 a.m. an 5 p.m., except as provided in § 261.8 of the Board's Rules Regarding Availability of Information, 12 CFR 261.8.

FDIC: Hoyle L. Robinson, Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street NW., Washington, DC 20429. Comments may be hand delivered to room F-402, 1776 F Street NW., Washington, DC, on business days between 8:30 a.m. and 5 p.m. Comments may also be inspected in room F-402 between 8:30 a.m. and 5 p.m. on business days. [FAX number (202) 898-3838]

OTS: Comments should be directed to Director, Information Services Division, Public Affairs, Office of Thrift Supervision, 1700 G Street NW., Washington, DC 20552, Attention: Docket No. [92-239]. These submissions may be hand delivered to 1770 G Street, NW., from 9 a.m. to 5 p.m. on business days; they may be sent by facsimile transmission to FAX number (202) 906-7753 or 7755. Submissions must be received by 5 p.m. on the day they are due in order to be considered by the OTS. Late-filed, misaddressed, or misidentified submissions will not be considered in this rulemaking. Comments will be available for inspection at 1776 G Street NW., Street Level.

FOR FURTHER INFORMATION CONTACT:

OCC: Emily R. McNaughton, National Bank Examiner (202/874-5170), Office of the Chief National Bank Examiner; Jeff Mace, Attorney, Securities and Corporate Practices Division (202/874-5210); Laura H. Plaze, Attorney, Legal Advisory Services Division (202/874-5330), Office of the Comptroller of the Currency, 250 E Street, SW., Washington, DC 20219.

Board of Governors: Roger Cole, Assistant Director (202/452-2618), David Wright, Supervisory Financial Analyst (202/728-5854), Division of Banking Supervision and Regulation; Scott G. Alvarez, Associate General Counsel (202/452-3583), Gregory A. Baer, Senior Attorney (202/452-3236), 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 and C Streets, NW., Washington, DC 20551.

FDIC: For supervisory issues, Robert F. Miailovich, Associate Director (202/898-6918) or Robert W. Walsh, Examination Specialist (202/898-6911), Division of Supervision, FDIC, 550 17th Street, NW., Washington, DC 20429; for legal issues, Lisa M. Stanley, Senior Attorney (202/898-7494), Jeffrey M. Kopchik, Counsel (compensation standards issues) (202/898-3872); or Nancy L. Alper, Counsel (compliance and enforcement issues) (202/898-3720), Legal Division, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

OTS: John C. Price, Jr., Deputy Assistant Director for Policy (202/906-5745), Robert Fishman, Program Manager (202/906-5672), Cherly Martin, Regional Coordinator (202/906-7869), Policy Office; V. Gerard Comizio, Deputy Chief Counsel for Securities and Corporate Structure (202/906-6411), James H. Underwood, Counsel (Banking and Finance) (202/906-7354), Chief Counsel's Office; Deirdre Kvartunas, Program Analyst, (202/906-7933), Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552.

SUPPLEMENTARY INFORMATION:

I. Background and Information

Section 132 of the FDICIA, Public Law No. 102-242, added a new section 39 to the Federal Deposit Insurance Act (FDI Act) which requires each of the agencies to prescribe by regulation certain safety and soundness standards for the insured depository institutions and depository institution holding companies for which it is the primary Federal regulator. Standards must be prescribed in three principal areas: (1) Operational and managerial; (2) asset quality, earnings, and stock valuation; and (3) employee compensation. If an insured depository institution does not meet one of these standards, section 39 requires that the institution establish a plan to achieve compliance with the standard that is acceptable to the primary regulator of the institution. Final regulations implementing section 39 must be promulgated no later than August 1, 1993, and become effective no later than December 1, 1993.

Various questions and issues have arisen involving general and specific

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aspects of the required regulatory safety and soundness standards. The agencies are issuing this joint advance notice of proposed rulemaking for the purpose of gathering public comment on these issues to assist them in the development of a proposed rulemaking. The agencies intend to work together in formulating the proposed and final rulemaking.

The agencies are interested in receiving comments concerning all aspects of section 39 of the FDI Act. The overriding issue facing the agencies in adopting regulations pursuant to section 39 of the FDI Act is how to balance the objectives of the statute relating to safety and soundness standards with the important need to avoid establishing unrealistic and overly burdensome standards that unnecessarily raise costs within the regulated community. In light of the need to attract and retain capital and management talent in the banking and thrift industries, it is important that the standards not needlessly impose uncertainty or raise substantive issues with respect to their implementation by the agencies going forward.

Section 39 does not require, and the agencies do not intend to prescribe, inflexible standards specifying how depository institutions must be managed. Rather, the agencies intend to prescribe standards designed to prevent institutions from developing serious problems and thereby prevent loss to the deposit insurance funds. Thus, for each safety and soundness standard, commenters are requested to recommend specific regulatory language that fulfills the intent of section 39 of the FDI Act while leaving management appropriate latitude and flexibility.

In order to elicit comment on certain issues identified by the agencies, specific questions are set forth that address each subsection of section 39 of the FDI Act. Commenters are requested to number their responses to correspond to the question number. Questions need not be repeated, and commenters may respond to as many questions as they wish. Where a comment recommends a particular recordkeeping or reporting requirement, the commenter is requested to include an estimate of the number of hours necessary for an institution or holding company to comply.

II. Operational and Managerial Standards

Section 39(a) of the FDI Act requires each of the agencies to prescribe for the institutions it regulates managerial and operational standards relating to:

- Internal controls, information systems, and internal audit systems;
- Loan documentation;
- Credit underwriting;
- Interest rate exposure;
- Asset growth;
- Compensation, fees, and benefits in accordance with subsection (c) of section 39; and
- Such other operational and managerial standards as the agency determines to be appropriate.

A. Internal Controls, Information Systems, and Internal Audit Systems

Internal controls, information systems, and internal audit systems are generally designed to achieve compliance with laws and regulations, safeguard assets, promote operational efficiency, and encourage adherence to prescribed managerial policies. Institutions may define these systems and controls differently.

(1) Should these items be defined in the regulation, and what, if any, specific standards should the regulation include?

The bank and thrift regulatory agencies, as well as accounting, auditing, banking and thrift associations and others, have published guidelines, opinions, advisories, and other literature on standards for internal controls, information systems and internal audit systems.

(2) Which, if any, of these preexisting standards should be incorporated into the regulation?

B. Loan Documentation

Each of the agencies currently reviews the loan files of the institutions it examines to determine the adequacy of loan documentation. The Office of Thrift Supervision has prescribed regulations that establish an item-by-item listing of loan documentation requirements. 12 CFR 563.170(c)(1).

(3) Should loan documentation standards for all financial institutions prescribe an item-by-item listing of requirements, or should loan documentation standards be general in nature and prescribe prudential documentation?

(4) Should documentation standards vary according to loan types or loan amounts, and, if so, how?

C. Credit Underwriting

The agencies currently review the credit underwriting standards established by each depository institution in the examination process. In implementing section 39 of the FDI Act, the agencies seek comment on whether the regulation must prescribe general standards or specific requirements. General credit underwriting standards could, for example, require institutions to adhere to prudent standards as specified by the institution's loan policies. More detailed credit underwriting standards could specify criteria—such as descriptions of collateral, cash flow coverage, working capital, and loan to value ratios—that should be employed in making sound credit decisions.

(5) Should the agencies prescribe general or specific underwriting standards?

(6) Should the regulation specify minimum acceptable ratios for credit underwriting criteria, and, if so, what minimum ratios would be appropriate?

Section 304(a) of FDICIA added a new section 18(o) to the FDI Act which requires each agency to adopt uniform regulations prescribing standards for extensions of credit related to real estate. FDICIA, section 304(a), 105 Stat. 2354 (12 U.S.C. 1828(o)). The agencies will also be promulgating regulations on section 304. Credit underwriting standards must also comport with the standards prescribed pursuant to this section.

(7) How should the agencies coordinate implementation of section 18(o) of the FDI Act with implementation of section 39?

D. Interest Rate Exposure

The FDICIA also requires the agencies to prescribe standards relating to interest rate exposure.

(8) How should interest rate exposure standards be defined and measured, and what should the standards prescribe?

(9) How and to what extent should the agencies consider the size of an institution or company in determining standards for interest rate exposure?

(10) Should the agencies consider the overall financial condition of the institution or company in establishing interest rate exposure standards, and if so, how?

Section 305(b) of the FDICIA requires each agency to revise its risk-based capital standards to ensure that those standards take adequate account of interest rate risk. FDICIA, section 305(b), 105 Stat. 2354.

(11) How does section 305(b) of the FDICIA affect the types of standards that need to be established pursuant to section 39 of the FDI Act?

E. Asset Growth

Under section 39 of the FDI Act, the agencies must prescribe standards relating to asset growth. The principal issues in prescribing asset growth standards are how asset growth should be defined and measured, and what limits, if any, should be established. The FDIC currently addresses "rapid growth" by requiring all insured depository institutions to give the

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appropriate FDIC regional director for supervision 30 days advance notice when planning to increase their assets by 7.5 percent or more during any three-month period through the solicitation, in any combination, of fully insured brokered deposits, fully insured out-of-territory deposits, or secured borrowings, including repurchase agreements. 12 CFR 304.6.

(12) What limits on asset growth should be established for purposes of section 39 of the FDI Act? Since a regulation to monitor rapid asset growth is in place, what other standards for asset growth, if any, should be prescribed under section 39?

(13) If other growth measures should be included, what should they consider? Should the regulation consider only the percentage change in total assets or also the mix and quality of asset growth?

(14) Should asset growth standards be different for depository institutions and depository institution holding companies?

(15) How should the agencies treat asset growth funding sources, supervisory ratings assigned by the primary regulator, and off-balance-sheet risk in establishing asset growth standards?

(16) Growth through merger is generally supervised by the agencies through applications received under the Bank Merger Act (12 U.S.C. 1828(c)), Bank Holding Company Act (12 U.S.C. 1941, *et seq.*), and Savings and Loan Holding Company Act (12 U.S.C. 1467a). Should standards for asset growth through merger be prescribed under section 39, and, if so, how?

(17) What is the appropriate time period for measuring asset growth—quarterly, yearly?

(18) Should asset growth standards differentiate between insitutions or companies based on factors such as capital adequacy, asset quality, or size, and, if so, how?

(19) Should the regulation permit exceptions, and, if so, under what circumstances?

III. Asset Quality, Earnings, and Stock Valuation Standards

Section 39(b) of the FDI Act requires each of the agencies to prescribe standards specifying:

- A maximum ratio of classified assets to capital;
- Minimum earnings, sufficient to absorb losses without impairing capital;
- To the extent feasible, a minimum ratio of market value to book value for publicly traded shares of the institution or company; and
- Such other asset quality, earnings, and valuation standards as the agency determines to be appropriate.

A. Asset Quality

The statute requires that the agencies incorporate "classified assets" in the ratio. The agencies currently have a joint policy that defines "classified assets" as those assets considered substandard, doubtful, or loss.

(20) Is this definition appropriate for purposes of section 39 of the FDI Act, or should classified assets be weighted or adjusted in some other manner in calculating the ratio—that is, to weigh the more adverse classifications more heavily, or to include additional problem assets?

(21) How should capital be defined for purposes of establishing a maximum ratio of classified assets to capital?

(22) Should maximum ratios vary depending on an institution's size, earnings, or other factors?

(23) What other factors should be considered in determining a maximum ratio of classified assets to capital?

(24) How should the ratio be defined to discourage institutions that are approaching the maximum ratio from understating problem assets?

B. Earnings

The statute requires that the agencies specify earnings sufficient to avoid impairing capital.

(25) What is the appropriate earnings measure and time period for determining whether minimum earnings have been achieved without impairing capital?

(26) How should the term "impairing capital" be defined—as an absolute reduction in capital, as a reduciton in capital below the minimum required capital ratios, as earnings insufficient to maintain capital ratios, or otherwise?

(27) Should the quality of earnings be taken into account, and, if so, what factors should be considered?

(28) How should the regulation address the potential incentive for manipulation of short term earnings?

(29) Should an institution that is part of a holding company be subject to different earnings standards than an institution that is not part of a holding company?

C. Market Value to Book Value

Section 39(b)(1)(C) of the FDI Act requires the agencies to prescribe standards specifying a minimum ratio of market value to book value for publicly traded shares, "to the extent feasible." The market price of depository institutions' publicly traded common stock, like the stock price of all companies, varies with the actual or perceived financial health and earnings power of the individual institution and the relative attractiveness of stocks in general as compared to alternative investments.

(30) Is a standard prescribing a minimum ratio of market value to book value feasible, and why or why not? Is it possible to adjust such a ratio for structural fluctuations in the stock market that may not be related to the market value of any individual depository institution's stock price? Would a minimum ratio of market value to book value encourage undesirable behavior by publicly traded depository institutions, and, if so, how may a ratio be defined to minimize such undesirable consequences?

(31) If a minimum ratio of market to book value were considered feasible, what should the minimum market to book ratio be? Should this ratio be tied to an industry or market index, and, if so, what index and how?

IV. Compensation Standards

Section 39(c) of the FDI Act requires each of the agencies to prescribe for the institutions it regulates standards for determining when compensation paid to officers, directors, employees, and principal shareholders of insured depository institutions is excessive. The agencies must also prescribe standards prohibiting as an unsafe and unsound banking practice any employment contract, compensation or benefit agreement, fee arrangement, perquisite, stock option plan, post-employment benefit, or other compensatory arrangement that either provides the recipient with excessive compensation, fees, or benefits, or could lead to material financial loss to the institution.

In prescribing these standards, the agencies must consider:

- The combined value of all cash and noncash benefits provided to the individual;
- The compensation history of the individual and other individuals with comparable expertise at the institution;
- The financial condition of the institution;
- Comparable compensation practices at comparable institutions;
- For post-employment benefits, the projected total cost and benefit to the institution;
- Any connection between the individual and any fraudulent act or omission, breach of trust or fiduciary duty, or insider abuse with regard to the institution; and
- Any other factors that the agency determines to be relevant.

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The agencies are concerned about achieving an appropriate balance between preventing excessive compensation, as the statute directs, and not unduly interfering with the business relationships between an institution and its officers, directors, and employees. In this regard, they have identified the following issues for consideration:

- Specificity of standards;
- "Excessive" based on performance and condition;
- "Excessive" based on form of compensation;
- "Excessive" based on connection to impropriety.
- "Compensation procedures and reviews;
- "Peer group comparisons; and
- Coverage of holding companies.

A. Specificity of Standards

Section 39 of the FDI Act requires the agencies to establish standards specifying what constitutes excessive compensation "by considering" the above factors enumerated by statute and any other factors the agency determines to be relevant.

(32) Do the statutory factors need further clarification by regulation, or are they sufficient to give notice of what would constitute excessive compensation? If the statutory factors are not sufficient, what additional factors should the agencies include in determining whether compensation is excessive?

(33) Do troubled institutions require more scrutiny of compensation than other institutions, and should different standards for excessive compensation be established for troubled institutions?

(34) Should the standards reflect that troubled institutions may have to offer higher compensation to attract and retain management to resolve their problems, and, if so, how?

The agencies are concerned about the usefulness of applying such a regulation to lower level, non-official personnel where the likelihood of abusive practices would seem to be very low.

(35) While the statute addresses the compensation of all officers, directors, employees, and principal shareholders, should the standards be more specific regarding the compensation of senior executive officers and directors?

B. "Excessive" Based on Performance and Condition

Section 39(c)(2)(C) of the FDI Act provides that unreasonable or disproportionate compensation shall be determined by considering, among other factors, the financial condition of the institution.

(36) How should the financial condition of the institution be considered in applying this standard?

(37) Could and should the regulation require that executive compensation be tied to and vary with an institution's profitability or its overall financial condition? If so, how should this be done? Should the agencies consider the supervisory rating assigned to an institution in determining its financial condition, or should other indicia of condition be considered? If the agencies were to consider profitability, how could this be done in a way that would not encourage management to sacrifice long term profitability for short term gain?

(38) Should the role of management in any deterioration of the financial condition of an institution be considered in applying this standard?

C. "Excessive" Based on Form of Compensation

The statute lists various forms of compensation to be considered in determining whether the compensation of a director, officer, or employee is excessive.

(39) Should the definition of "excessive" vary according to the form of compensation to be received—for example, cash versus stock options? Should items of compensation be considered individually or in the aggregate?

(40) How should the agencies construe the word "perquisite" as it is used in section 39(c)(1) of the FDI Act? Should this term encompass preferential non-credit transactions and deposit accounts provided to officers, directors, and employees?

(41) Should the agencies establish different standards for what constitutes excessive compensation for outside directors—that is, directors who are not employees or officers?

D. "Excessive" Based on Connection to Impropriety

The statute requires the agencies to consider "any connection between the individual and any fraudulent act or omission" in determining whether an individual's compensation is excessive.

(42) How should the agencies interpret this requirement?

E. Compensation Procedures and Reviews

In complying with the compensation standards, institutions will need to determine and monitor the total compensation of their directors, officers, and employees.

(43) Should the agencies define "employment agreement," and, if so, how?

(44) Should employment agreements between institutions and executive officers and directors be required to be in writing?

(45) Should the institution's compensation records indicate all related direct and indirect payments, fees, and benefits which are provided to an executive officer?

(46) Should the institution's board of directors be required to review and approve all executive officer compensation?

F. Peer Group Comparisons

In arriving at compensation standards, section 39(c)(2)(D) of the FDI Act requires the agencies to consider a peer group comparison of compensation at comparable institutions defined by geographic location, asset size, and the complexity of the loan portfolio or other assets.

(47) Is information currently available to the industry through private data vendors sufficient for the industry and regulators to determine whether the compensation paid by a depository institution to its officers, directors, employees, and principal shareholders is comparable to the levels paid by comparable institutions? If not, what additional information would need to be gathered, from whom, and how?

G. Coverage of Holding Companies

Section 39(a) of the FDI Act requires that various operational and managerial standards be established for both insured depository institutions and depository institution holding companies, including standards for compensation "in accordance with subsection (c)." Section 39(c) of the FDI Act requires the agencies to prescribe compensation standards only "for all insured depository institutions." Accordingly, the agencies do not believe that they are required to prescribe compensation standards for depository institution holding companies.

(48) Should the agencies construe the statute as requiring the establishment of compensation standards for depository institution holding companies? Would this interpretation, or a contrary interpretation, create anomalies or problems in applying the statute?

V. Failure to Meet Prescribed Standards

Section 39(e) of the FDI Act requires an institution to submit an acceptable plan to the appropriate Federal banking agency whenever the agency determines that the institution has failed to meet any of the safety and soundness

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standards prescribed under subsections (a), (b), and (c) of section 39.

Plans must specify the steps the institution will take to correct the deficiency. Plans must be submitted within a reasonable time, as established by the agency, and generally not later than 30 days after the agency determines that the institution fails to meet a prescribed safety and soundness standard.

In the event that an institution fails to submit an acceptable plan within the time allowed or fails in any material respect to implement an accepted plan, section 39(e)(2) of the FDI Act requires the appropriate agency to issue an order requiring the institution or company to correct the deficiency, and authorizes the agency to take various other actions until the deficiency has been corrected. These actions include limiting asset growth, restricting interest rates paid, requiring an increase in the ratio of tangible equity to assets, and other actions that the agency determines will better carry out the purpose of section 38 of the FDI Act (prompt corrective action). Agencies are required to take certain of these actions whenever an institution fails to meet a prescribed standard and either has commenced operations or experienced a change in control during the 24-month period preceding the institution's failure to meet the standard, or has experienced extraordinary asset growth during the 18-month period preceding the institution's failure to meet the standard.

The agencies are concerned that the sanctions imposed on an institution not in compliance with a prescribed regulatory standard be consistent with the safe and sound operation of the institution. For example, a requirement to increase tangible equity to assets may induce certain institutions to shrink their balance sheets and could thereby adversely affect safety and soundness by increasing an institution's risk.

(49) How can the agencies avoid this risk?

Agencies monitoring compliance with the safety and soundness standards prescribed under section 39 of the FDI Act will rely on examinations, financial reports, and other tools, but will often not be able to determine immediately when an institution has failed to comply with those standards.

(50) Should a depository institution or depository institution holding company be required to notify its primary regulator when it has failed to comply with a safety and soundness standard under section 39? Would such a requirement aid enforcement of the statute? Would requiring such notification have any undesirable effects?

VI. Additional Standards

Section 39 of the FDI Act authorizes the agencies to prescribe safety and soundness standards relating to operation and management, asset quality, earnings, and stock valuation, and employee compensation, in addition to those enumerated in the statute.

(51) The agencies request comment on whether additional standards are necessary and feasible, and if so, which areas should be addressed and what standards should be implemented.

VII. Holding Company Role

The agencies anticipate that, in order to promote efficiency and cut costs, multi-bank or thrift holding companies may wish to establish safety and soundness standards for all their subsidiary institutions. So long as the standards are ratified by the board of the subsidiary institutions, the agencies believe that this procedure is a reasonable means of complying with the requirements of section 132 of FDICIA.

(52) Is such a procedure an adequate and advantageous way of complying with section 132 of FDICIA?

VIII. Relationship to Other Statutory Provisions

Section 39 of the FDI Act requires the agencies to prescribe safety and soundness standards by regulation in certain areas. Several other statutory provisions pertain to the same or similar safety and soundness standards—for example, section 304 of the FDICIA requires restrictions on real estate lending. Where appropriate, commenters are requested to specify how their interpretation of section 132 relates to other sections of FDICIA.

IX. Issues Relating to Thrifts and Savings and Loan Holding Companies

The OTS particularly solicits comment on the application of these safety and soundness standards to savings and loan holding companies. The Home Owners' Loan Act provides significant flexibility to unitary savings and loan holding companies whose thrift subsidiaries meet the "Qualified Thrift Lender" test and, in the case of multiple savings and loan holding companies, where all, or all but one, of the thrift subsidiaries were acquired in a supervisory transaction. These savings and loan holding companies (unlike similarly structured bank holding companies) may generally engage in any type of activity. This activity flexibility permits a wide range of commercial and industrial firms to become diversified savings and loan holding companies. With these companies, only a small portion of their overall business may consist of the thrift and its activities.

The OTS's regulation of thrift holding companies concentrates on ensuring that subsidiary thrifts are well-managed and well-capitalized and that transactions and relationships between thrifts and their holding companies satisfy fiduciary requirements and do not negatively affect the thrift's safety and soundness. The OTS has not sought to regulate the way a holding company conducts its nonthrift business if these fundamental objectives are being met.

The OTS requests comment on the application of the Operational and Managerial Standards (Section II, above) and the Asset Quality, Earnings, and Stock Valuation Standards (Section III, above) to all savings and loan holding companies and requests that commenters address the following questions:

(53) Should the OTS's standards for savings and loan holding companies differ from the bank regulatory agencies' standards for bank holding companies and, if so, how?

(54) Should the OTS set different standards for diversified savings and loan holding companies versus non-diversified savings and loan holding companies and, if so, how?

(55) Should different standards be set for operating versus "shell" holding companies?

X. Differential Regulation

The agencies request comment on the extent to which the regulatory standards for the areas described above should vary based on an institution's financial and managerial condition. The agencies request that commenters address this issue in their responses to the questions listed above.

By Order of the Board of Governors of the Federal Reserve System.

Dated: June 26, 1992.

Jennifer J. Johnson,

Associate Secretary of the Board.

[FR Doc. 92-16576 Filed 7-14-92; 8:45 am]

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