

DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

12 CFR Parts 541, 545, 560, 561

[No. 99-34]

RIN 1550-AB21

Letters of Credit, Suretyship and Guaranty

AGENCY: Office of Thrift Supervision, Treasury.

ACTION: Final rule.

SUMMARY: The Office of Thrift Supervision (OTS) is amending its regulations to clarify that a Federal savings association may act as guarantor under section 5(b)(2) of the Home Owners' Loan Act (the "HOLA"). Additionally, OTS is modifying restrictions on suretyship and guaranty agreements issued under this section. The rule also clarifies that a Federal savings association holds authority to issue letters of credit and makes related technical amendments. OTS is also amending various lending related definitions to either clarify definitions or remove unnecessary or outdated definitions.

EFFECTIVE DATE: October 1, 1999.

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SUPPLEMENTARY INFORMATION:

I. Background

On September 18, 1998, OTS issued a Notice of Proposed Rulemaking ("NPR") clarifying a Federal savings association's authority to act as guarantor under section 5(b)(2) of the HOLA. The proposed rule included restrictions on suretyship and guaranty agreements issued under this authority. OTS also proposed revisions clarifying that Federal savings associations may issue letters of credit. Finally, OTS sought comment on whether it should adopt a regulation to address the escrow authority of Federal savings associations.

This document finalizes the proposed changes, clarifies or removes various related definitions that are outdated or unnecessary, and makes other technical amendments.

II. Summary of Comments

The public comment period on the NPR closed on November 17, 1998. Two Federal savings associations, two trade associations, a Federal Home Loan Bank, and one individual filed comments on the NPR.

Four commenters addressed OTS's proposal clarifying the guaranty authority for Federal savings associations and proposing restrictions on suretyship and guaranty agreements under section 5(b)(2) of the HOLA. Two commenters supported the proposed changes and two commenters suggested clarifications.

Two commenters supported the clarification of the authority of Federal savings associations to issue letters of credit. Three commenters opposed the issuance of a regulation addressing the escrow authority of Federal savings associations. OTS has addressed the specific comments in the section-by-section discussion below.

III. Section-by-Section Discussion

A. Suretyship and Guaranty¹

Section 5(b)(2) of the HOLA provides “[t]o such extent as the Director may authorize in writing, a Federal savings association . . . may be surety as defined by the Director”² OTS's current regulation at 12 CFR 545.103 authorizes Federal savings associations to act as surety under this section, subject to specified conditions.

Neither section 5(b)(2) of the HOLA nor current § 545.103 address a Federal savings association's authority to issue a guaranty.³ Nonetheless, OTS and its predecessor,

¹ Letters of credit and other independent undertakings are discussed in Section III. B. below.

² 12 U.S.C. 1464(b)(2).

³ Under a suretyship agreement, the surety is bound with its principal to pay or perform an obligation to a third party. BLACK'S LAW DICTIONARY 1441-42 (6th ed. 1990). Under a guaranty agreement, on the other hand, the guarantor

the Federal Home Loan Bank Board (“FHLBB”), have recognized that the authority of a Federal savings association to act as guarantor is subsumed within section 5(b)(2) of the HOLA.⁴ To clarify this point, OTS proposed to specifically authorize Federal savings associations to act as guarantors. OTS also proposed to move the portion of the regulation authorizing surety and guaranty agreements under section 5(b)(2) of the HOLA from Part 545 to the lending and investment regulation at Part 560.

Currently § 545.103 imposes various conditions on the exercise of a Federal savings association’s authority under section 5(b)(2) of the HOLA. Under these conditions, a Federal savings association may enter into a surety agreement only if its performance under the agreement would create an obligation authorized for investment and it takes and maintains a perfected security interest in described collateral. In addition, the current rule treats the obligation under the surety agreement as a loan to the principal under the loans-to-one-borrower limits and loans to insider restrictions.

OTS proposed several modifications to these existing conditions. First, OTS proposed to revise the collateral requirements to reflect changes to the Office of Comptroller of the Currency’s (OCC) related regulation on surety and guaranty

agrees to satisfy the obligation of the principal to another only if the principal fails to pay or perform. *Id.* at 705.

⁴ See *e.g.*, 48 FR 23032, 23043 (May 23, 1983) (stating that section 5(b)(2) of the HOLA empowers the FHLBB to authorize by regulation the issuance of suretyship devices by Federal savings associations for the purpose of guarantying the obligations of others); FHLBB Op. Assoc. Gen. Counsel (July 5, 1983) (permitting the association to act as surety or guarantor under section 5(b)(2) of the HOLA). See also 12 CFR 545.16(a)(3) (“surety” means surety under real and/or personal suretyship, and includes guarantor).

agreements.⁵ Second, OTS proposed to add a new provision requiring the association to limit its obligations under the surety or guaranty agreement to a fixed amount and a specified duration. The proposed rule also added definitions of the terms suretyship and guaranty agreement.⁶

Four commenters addressed the proposed surety and guaranty regulation. Two supported the proposed changes. Two other commenters suggested clarifications and changes. These two commenters argued that the text of the proposed rule assumes that all guaranties are repayable and, thus, treats all guaranty agreements as if they were loans. The commenters noted that many guaranty-type arrangements issued by savings associations are not repayable. As examples of such arrangements, the commenters cited letters of credit, recourse transactions, and various other corporate undertakings in financial transactions. The commenters urged OTS to adopt a rule recognizing the standard market practice of non-repayable guaranties and similar arrangements, and clarifying that these practices are not subject to the conditions contained in the proposed rule.

OTS did not intend to deprive Federal thrifts of any existing authority. Rather, like the existing rule, this provision is intended to address only repayable guaranty and surety

⁵ 12 CFR 7.1017, as amended by 61 FR 4849 (February 9, 1996).

⁶ The agency proposed to delete certain provisions of existing § 545.103. For example, current § 545.103(c) states that if a Federal savings association is required to perform under the suretyship agreement, it must treat the amount advanced as an extension of credit, subject to investment limits and other restrictions applicable to such an extension of

agreements issued under section 5(b)(2) of the HOLA.⁷ Federal savings associations hold other authority to issue other guaranties and guaranty-like arrangements. For example, a Federal savings association may sell loans with recourse,⁸ issue letters of credit and other independent undertakings,⁹ and act as a surety for public deposits.¹⁰ Further, a Federal savings association may execute signature guaranties,¹¹ may act as a surety with respect to its lost or destroyed Government National Mortgage Association (GNMA) certificate,¹² and may offer performance guaranties on low down payment mortgage loans that it originates or purchases and insures with a private mortgage insurer.¹³ OTS did not intend to limit these authorities or to subject these authorities to the conditions contained in the proposed rule.

credit. OTS has deleted this paragraph because it duplicates § 560.31(a).

⁷ See FHLBB Op. Gen. Counsel (March 5, 1985)(Section 545.103 “addresses the situation where the association for a fee backs the obligation of another to a third party; the party contracting for the association to pledge to pay its debt would be liable to the association for repayment should the association have to make payment to the third party under the surety agreement.”)

⁸ See 47 FR 4049, 4051 (January 28, 1982).

⁹ See today’s final rule at § 560.50.

¹⁰ 12 CFR 545.16.

¹¹ See FHLBB Op. Gen. Counsel (August 11, 1981)(“The authority to guarant[y] customer signatures is both implied in and incidental to the express objects and powers of Federal associations as set forth in the HOLA and the Federal charter.”).

¹² See FHLBB Op. Gen. Counsel (March 5, 1985)(“This is a form of offering the association’s assets generally in support of its obligations which appears to be incidental to its authority to enter into the GNMA transaction and to give security.”).

¹³ See OTS Op. Chief Counsel (October 2, 1998)(This activity “is subsumed within the residential real property lending authority of Federal savings associations in section 5(c)(1)(B) of the [HOLA], and is a power incident to this authority.”).

OTS has revised its final rule to clarify this point. The final rule clarifies that a Federal savings association may enter into a repayable suretyship or guaranty agreement under section 5(b)(2) of the HOLA, subject to the conditions listed in § 560.60.

As noted in the NPR, OTS modeled its rule on the OCC's rule on surety and guaranty agreements at 12 CFR 7.1017. The OCC's regulation states that:

A national bank may lend its credit, bind itself as a surety to indemnify another, or otherwise become a guarantor, if: (a) The bank has a substantial interest in the performance of the transaction involved . . . ; or (b) The transaction is for the benefit of a customer and the bank obtains from the customer a segregated deposit that is sufficient in amount to cover the bank's total potential liability.

One commenter observed that the proposed rule incorporated paragraph (b), but did not incorporate paragraph (a) of the OCC's rule. Thus, the commenter noted that OCC does not require a national bank to collateralize the transaction or meet collateral requirements listed in paragraph (b), if the bank holds a substantial interest. The commenter, therefore, asserted that OTS has imposed more rigorous requirements than OCC, causing the thrift charter to be less attractive than the national bank charter.

OCC appears to have included the "substantial interest" provision to clarify the authority of national banks in light of judicial precedent limiting their ability to issue guaranties for others based on a lack of express authority to national banks to guarantee the

acts of third parties.¹⁴ Despite this limitation, national banks may provide guaranties that are “entered into for the furtherance of their own rights or as an incident to the transaction of business.”¹⁵ Interpretative Ruling 7.1017 was “intended to provide a general statement of this incidental powers exception to the general prohibition against national banks’ entering guaranties.”¹⁶ Because the HOLA expressly authorizes thrifts to enter into suretyship and guaranty agreements,¹⁷ it is unnecessary to include a similar clarification in OTS’s authorizing rule.

Moreover, OTS believes that a new paragraph incorporating incidental powers concepts would duplicate other existing OTS regulations. Like national banks, federal savings associations hold powers incident to their express powers, as set forth in the HOLA.¹⁸ OTS regulations at 12 CFR 544.1 and 552.3 already state that a Federal savings association may “exercise all the express, implied, and incidental powers conferred” by the HOLA. In light of this general recognition of incidental powers under the HOLA, OTS has not restated the widely recognized incidental powers concepts in this authorizing rule.

¹⁴ See OCC Unpublished Interpretative Letter (June 4, 1993) citing Dunn v. McCoy, 113 F.2d 587, 588 (3d Cir. 1940); Kimen v. Atlas Exch. Nat’l Bank, 92 F.2d 615, 617 (7th Cir. 1937), cert. denied, 303 U.S. 650 (1938); Border Nat’l Bank v. American Nat’l Bank, 282 F. 73, 77 (5th Cir.), cert. denied and appeal dismissed, 260 U.S. 701 (1922); Bowen v. Needles Nat’l Bank, 94 F. 925, 927 (9th Cir. 1899), cert. denied, 176 U.S. 682 (1900).

¹⁵ OCC Interpretative Letter 376 (October 22, 1986), citing Dunn, 113 F.2d at 589.

¹⁶ OCC Unpublished Interpretative Letter (June 4, 1993).

¹⁷ See 12 U.S.C. 1464(b)(2) and infra notes 2-4 and accompanying text.

¹⁸ See OTS Op. Acting Chief Counsel (March 25, 1994) at 7-8 and (October 17, 1994) at 4-5.

In the proposed rule, OTS asked whether the OTS rule should specifically authorize other types of suretyship, guaranty, or similar arrangements beyond those covered in the proposed rule. One commenter recommended that OTS adopt a rule based on the OCC's former rule at 12 CFR 7.7015 (1996), which permitted a national bank to engage in check guaranty plans under which it will honor checks drawn on it up to a certain amount. OCC determined that this arrangement is essentially a credit agreement and, therefore, a permissible activity.

OTS believes that the HOLA expressly authorizes these check guaranty plans. A check guaranty plan is an arrangement where an institution holds out to the public that it will honor checks drawn upon it up to a certain amount by a depositor who displays a check guaranty card. A check guaranty plan is, in essence, an agreement by a Federal savings association to pay deposits out of an account or extend credit up to a predetermined amount to a depositor when insufficient funds are available to honor a check drawn on a depositor's account.¹⁹ In the latter case, such a commitment to lend is within the express powers of Federal savings associations under section 5(c)(1)(A) of the HOLA, which permits a Federal savings association to make "loans specifically related to transaction accounts."²⁰ OTS regulation at 12 CFR 560.30, which implements this section of the

¹⁹ OCC reached a similar conclusion that check guaranty plans are essentially a loan commitment. See 12 CFR 7.7015 (1996).

²⁰ 12 U.S.C. 1464(c)(1)(A). Moreover, section 12 of the HOLA expressly authorizes a Federal savings association to advertise, subject to OTS regulations.

HOLA, specifically states that transaction account loans include overdrafts.²¹ Thus, the HOLA and OTS regulations already authorize a Federal savings association to offer a plan that provides a line of credit on the customer's checking account. Since a Federal savings association may make overdraft loans, it is not necessary to expressly authorize check guaranty plans in the revised suretyship and guaranty provisions.²²

Today's final rule also includes several changes to the proposed rule. First, OTS has moved the conditions on the exercise of this surety and guaranty authority from its proposed location at § 560.115 to the authorizing provision at § 560.60.²³ Second, OTS has made minor clarifying revisions to the text of the rule. For example, OTS has revised the provision addressing real estate collateral at § 560.60(c)(1)(i) to require an evaluation or appraisal of real estate consistent with OTS appraisal regulation at 12 CFR 564.3. OTS has also replaced the phrase "prior mortgage" in § 560.60(c)(1)(i) with the phrase "any existing senior mortgages" to clarify this provision.

²¹ While loans on transactional accounts under section 5(c)(1)(A) of the HOLA are not subject to percentage of assets limitation, OTS implementing regulation indicates that "[overdrafts] on commercial deposit or transaction accounts shall be considered to be commercial loans for the purposes of determining the association's percentage of assets limitations." 12 CFR 560.30, footnote 20.

²² OTS notes that OCC removed the interpretive ruling on check guaranty plans from its regulations in 1996 because the ruling was unnecessary or repetitive. 61 FR 4849, 4860 (February 9, 1996).

²³ OTS originally placed these conditions in subpart B of part 560 to ensure that similar guaranty and surety agreements by state-chartered savings associations would be subject to cited conditions. A state-chartered savings association may not engage as principal in any type of activity that is not permissible for a Federal savings association, unless the FDIC has made certain determinations regarding the risk of the transactions. See 12 U.S.C. 1831e(a) (1989). Accordingly, this purpose will be preserved by placing the restrictions in the authorizing provision at § 560.60.

B. Letters of Credit and Other Independent Undertakings

Proposed § 560.50 would clarify that Federal savings associations are authorized to issue letters of credit, and may issue such other independent undertakings as are approved by OTS, subject to restrictions in existing § 560.120.²⁴ Three commenters addressed proposed § 560.50. Two of these commenters supported OTS's proposal. The third commenter submitted information regarding international practices relating to standby letters of credit. Today's final rule adopts proposed § 560.50 without change.

Today's final rule also makes several technical and clarifying revisions to § 560.120, a related rule on Letters of Credit and Other Undertakings to Pay Against Documents. First, OTS has redrafted paragraph (a) to be more concise. Second, OTS is revising footnote 1 to indicate that the U.N. General Assembly adopted in 1995 and the United States signed in 1997, the United Nations Convention on Independent Guarantees and Standby Letters of Credit. Third, OTS is revising § 560.120(b)(2)(ii) to clarify that the precautions on allowing credit assessments when an independent undertaking is renewed apply only to automatic renewals. Discretionary renewals implicitly allow the savings association to make any necessary credit assessment before renewing. Fourth, OTS is updating a telephone number in footnote 1.

²⁴ The broad scope of the term "independent undertakings" and its recent evolution require close supervision and review when such undertakings fall outside the more traditional activities generally known as letters of credit. OTS approval may take the form of legal opinions, general guidance, or case-by-case approvals, depending on how the undertakings are presented to the agency. See 63 FR 49874, 49875-76 (September 18, 1998).

OTS did not address these changes in the NPR. Because these changes are technical, rather than substantive, OTS has concluded that notice and public comment on these changes is unnecessary and contrary to the public interest.²⁵

C. Escrow Accounts

In the NPR, OTS requested comment on the escrow authority of Federal savings associations. OTS has long recognized that the authority of Federal savings associations to make loans includes the authority to establish an escrow account in connection with a loan.²⁶ However, OTS questioned whether it should clarify the scope of Federal savings associations' authority to handle escrow accounts that are not related to loans. OTS did not propose any new regulatory text on escrow accounts. Rather, it requested comment on this issue. OTS specifically asked commenters to address whether OTS should place any restriction on the exercise of the escrow authority.

Three commenters opposed the adoption of any regulation addressing the escrow authority of Federal savings associations. These commenters argued that current guidance in the escrow area is sufficient.²⁷ Commenters also feared that additional restrictions on

²⁵ See 5 U.S.C. 553(b)(B).

²⁶ See 61 FR 50951, 50961 (September 30, 1996).

²⁷ See 61 FR 50951, 50961 (September 30, 1996)(the authority to hold escrow accounts related to loans); OTS Regulatory Handbook: Trust Activities, § 140 (1992) and Op. Chief Counsel (October 17, 1995) (the authority to engage in fiduciary activities involving non-discretionary activities such as escrow or safekeeping services or acting as a custodian or paying agent); and OTS Op. Chief Counsel (August 19, 1998) (the authority to hold an escrow account for funds representing down-payments on vacations for a Federal savings association customer, a vacation organizer).

the exercise of escrow authority, particularly for escrow accounts related to loans, could lead to confusion with other regulations.²⁸

In light of these comments, OTS will not adopt a regulation on escrow authority in this rulemaking. OTS will continue to answer any questions that arise in this area on a case-by-case basis.

IV. Related Definitions

In connection with today's final rule, OTS has removed or revised certain lending-related definitions in Parts 541 and 561 and elsewhere. These revisions fulfill, in part, promises made in the final lending and investment regulation in 1996. In that rulemaking, OTS recognized that its regulations include similar, but not identical, terms in various regulatory provisions. OTS indicated that it would review its definitions and would minimize or eliminate the potential for confusion in a later rulemaking.²⁹

OTS did not address the possibility of these changes in the NPR. Nonetheless, OTS has concluded that additional notice and public comment on these changes is unnecessary and contrary to the public interest.³⁰ OTS has not made any substantive revisions in this

²⁸ See e.g., the Real Estate Settlement Procedures Act at 12 U.S.C. 2601 et seq. and the implementing regulations at 24 CFR 3500 et seq.

²⁹ See e.g., 61 FR 50951, 50953, 50959 (September 30, 1996).

³⁰ See 5 U.S.C. 553(b)(B).

final rule. Rather, OTS has simply removed some unused terms, and made other minor technical or clarifying changes to other definitions. OTS has made the following revisions:

A. Guaranteed loan, guaranteed obligation, and insured loan

The current OTS rules at Parts 541 and 561 include one definition of “guaranteed obligation” (§ 561.21), two definitions of “guaranteed loan” (§§ 541.13 and 561.20), and two definitions of “insured loan” (§§ 541.17 and 561.25). The FHLBB originally adopted these definitions between 1949 and 1968 to implement various lending and investments authorities then applicable to Federal savings associations.³¹ Neither OTS nor the FHLBB substantively revised these definitions after 1971. OTS merely adopted these definitions without change when it transferred and re-codified FHLBB regulations in 1989.³²

The current definitions of the cited terms conflict. For example, § 541.13 defines “guaranteed loan” as a loan guaranteed under the Servicemen’s Readjustment Act of 1944 or chapter 37 of title 38, United States Code, as amended. Section 561.20, on the other hand, defines “guaranteed loan” as a loan guaranteed under “(a) The Servicemen’s Readjustment Act of 1944 or chapter 37 of title 38, United States Code; (b) The New Communities Act of 1968; (c) Section 221 or section 224 of the Foreign Assistance Act of 1961, as in effect prior to December 30, 1969; or (d) Section 221 or section 222 of the

³¹ See 14 FR 3981 (July 16, 1949); 23 FR 9891 (December 23, 1958); 33 FR 16555 (November 14, 1968).

³² 54 FR 49411 (November 30, 1989).

Foreign Assistance Act of 1961, as in effect on December 30, 1969, and thereafter.” The two definitions of insured loans are similarly inconsistent.³³ These inconsistencies have arisen over time as the statutes and regulations affecting savings associations have been reorganized and recodified.

OTS regulations use the three cited terms only in the lending and investment chart at § 560.30. This chart expressly cross-references the explicit statutory citation for each type of guaranteed loan, guaranteed obligation, or insured loan. These cross-references completely and accurately define the scope of the lending and investment authority of Federal savings associations. Accordingly, OTS has concluded that these definitions are unnecessary and potentially confusing, and has deleted these provisions.

B. Open-end consumer credit and closed-end consumer credit

The current rules at §§ 561.36 and 561.10 define open-end consumer credit and closed-end consumer credit by a cross-reference to Regulation Z (12 CFR 226.2). OTS regulations use these two phrases only in § 560.3 (definition of consumer loan). Accordingly, OTS has deleted the definitions of open-end and closed-end consumer credit, and has revised 560.3 to include appropriate cross-references to Regulation Z.

³³ Compare 12 CFR 541.17 with 12 CFR 561.25.

OTS has also made a minor technical change to the definition of consumer loan at § 560.3. The existing consumer loan definition excludes “credit extended in connection with credit cards and bona fide overdraft loans.” OTS excluded these loans to reflect the fact that credit card loans and overdraft loans are not subject to the 35 percent of asset limitation applicable to consumer loans under section 5 of the HOLA.³⁴ OTS notes, however, that other types of loans may meet the technical definition of consumer loan at § 560.3, but may also be made without limitation under other sections of the HOLA. Examples include educational loans and home improvement loans.³⁵ OTS has revised the rule to indicate that the term consumer loan does not include credit extended in connection with credit card loans, bona fide overdraft loans, and other loans that the savings association has designated as made under investment or lending authority other than section 5(c)(2)(D) of the HOLA.³⁶

C. Residential real estate and related definitions

OTS has also made minor revisions to the definition of residential real estate and related definitions. Two changes consolidate defined terms. For example, § 541.3 defines the phrase “combination of home and business property” as a home used in part for business. OTS regulations use this phrase twice--once in the definition of residential

³⁴ See 61 FR 50951, 50959 (September 30, 1996). A Federal thrift’s aggregate investments in consumer loans, corporate debt securities, and commercial paper are subject to a 35 percent of assets limitation.

³⁵ 12 U.S.C. 1464(c)(1)(J) and (c)(1)(U).

³⁶ See 12 CFR 560.31.

real estate at § 541.23 and once in the definition of home loan at § 560.3. The final rule deletes § 541.3 and modifies §§ 541.23 and 560.3 accordingly.

Similarly, § 541.4 defines the phrase “combination of residential real estate and business property involving only minor or incidental business use” as residential real estate for which no more than twenty percent of the total appraised value of the real estate is attributable to the business use. OTS regulations use this phrase only in the definition of residential real estate at § 541.23. OTS has deleted § 541.4 and has revised § 541.23 to include the phrase.

In addition, § 541.23 currently defines residential real estate, in part, as “homes (including condominiums and cooperatives).” OTS has clarified the parenthetical phrase to include “a dwelling unit in a multi-family residential property such as a condominium or a cooperative.”³⁷

D. Miscellaneous definitions

Section 561.23 defines the term “home mortgage.” OTS regulations use this term only within the phrase “home mortgage loan” in Part 563e - Community Reinvestment. OTS has separately defined “home mortgage loan” for Part 563e by a cross-reference to the Federal Reserve Board’s Regulation C - Home Mortgage Disclosure.³⁸ Since OTS

³⁷ OTS has made a related change to the definition of home loan at 12 CFR 560.3.

³⁸ See 12 CFR 563e.12(l), which cross-references 12 CFR 203.2.

rules do not use the term “home mortgage” elsewhere, OTS has deleted this definition as superfluous.

OTS regulations define the phrase “normal lending territory” at § 561.32, but do not use this term anywhere. This definition appears to be a remnant of provisions found in former section 5(c) of the HOLA, which generally restricted real estate lending by a Federal savings association to property located in the state in which the association’s home office was located, or within 100 miles of the home office.³⁹ OTS has deleted this term as unnecessary.

The rules define “cooperative housing development” at § 541.6. This term, however, is also not used in OTS regulations. OTS has, therefore, deleted this definition.

OTS rules at § 561.11 define “closing date” as “any annual or semiannual closing date.” Three OTS regulations use this term. The cited definition is clearly inapplicable in two of these regulations. See 12 CFR 563b.7(g)(5)(the closing date of a public offering) and 12 CFR 567.4(a)(4)(the closing date for a response to a notice of intent to issue a capital directive). The remaining regulation at § 563b.3(f)(5) uses closing date within the phrase “annual closing date.” OTS, therefore, has removed this term as superfluous.

³⁹ 12 U.S.C. 1464(c)(1976).

V. Executive Order 12866

The Director of OTS has determined that this final rule does not constitute a “significant regulatory action” for the purpose of Executive Order 12866.

VI. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act, OTS certifies that this final rule will not have a significant economic impact on a substantial number of small entities. Today’s final rule will not impose any additional burdens or requirements on small entities. Rather, the final rule simply clarifies the authority of Federal savings associations to act as guarantor and to issue letters of credit. This final rule also streamlines lending related definitions or removes unnecessary or outdated definitions. While the final rule also restricts the circumstances under which savings associations may enter into surety and guaranty agreements, the restrictions are the minimum necessary for safe and sound operations and should not impose a significant burden on small savings associations.

VII. Unfunded Mandates Act of 1995

Section 202 of the Unfunded Mandates Reform Act of 1995, Pub. L. 104-4 (Unfunded Mandates Act), requires that an agency prepare a budgetary impact statement before promulgating a rule that includes a Federal mandate that may result in expenditure

by state, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. OTS has determined that the final rule will not result in expenditures by state, local, or tribal governments or by the private sector of \$100 million or more. Accordingly, this rulemaking is not subject to section 202 of the Unfunded Mandates Act.

List of Subjects

12 CFR Part 541

Savings associations.

12 CFR Part 545

Accounting, Consumer protection, Credit, Electronic funds transfers, Investments, Reporting and recordkeeping requirements, Savings associations.

12 CFR Part 560

Consumer protection, Investments, Manufactured homes, Mortgages, Reporting and recordkeeping requirements, Savings associations, Securities.

12 CFR 561

Savings associations.

Accordingly, the Office of Thrift Supervision amends chapter V, title 12, Code of Federal Regulations as set forth below:

PART 541 - DEFINITIONS

1. The authority citation for part 541 continues to read as follows:

Authority: 12 U.S.C. 1462a, 1463, 1464.

§§ 541.3, 541.4, 541.6, 541.13, 541.17 [Removed]

2. Sections 541.3, 541.4, 541.6, 541.13, and 541.17 are removed.

3. Section 541.23 is revised to read as follows:

§ 541.23 Residential real estate.

The terms residential real estate or residential real property mean:

(1) Homes (including a dwelling unit in a multi-family residential property such as a condominium or a cooperative);

(2) Combinations of homes and business property (i.e., a home used in part for business);

(3) Other real estate used for primarily residential purposes other than a home (but which may include homes);

(4) Combinations of such real estate and business property involving only minor

business use (i.e., where no more than 20 percent of the total appraised value of the real estate is attributable to the business use);

(5) Farm residences and combinations of farm residences and commercial farm real estate;

(6) Property to be improved by the construction of such structures; or

(7) Leasehold interests in the above real estate.

PART 545 [Amended]

PART 560 - LENDING AND INVESTMENT

4. The authority citation for part 560 continues to read as follows:

Authority: 12 U.S.C. 1462, 1462a, 1463, 1464, 1467a, 1701j-3, 1828, 3803, 3806; 42 U.S.C. 4106.

§ 545.103 [Redesignated as § 560.60]

5. Section 545.103 is redesignated as § 560.60 and revised to read as follows:

§ 560.60 Suretyship and guaranty.

Pursuant to section 5(b)(2) of the HOLA, a Federal savings association may enter into a repayable suretyship or guaranty agreement, subject to the conditions in this section.

(a) What is a suretyship or guaranty agreement? Under a suretyship, a Federal savings association is bound with its principal to pay or perform an obligation to a third

person. Under a guaranty agreement, a Federal savings association agrees to satisfy the obligation of the principal only if the principal fails to pay or perform.

(b) What requirements apply to suretyship and guaranty agreements under this section? A Federal savings association may enter into a suretyship or guaranty agreement under this section, subject to each of the following requirements:

(1) The Federal savings association must limit its obligations under the agreement to a fixed dollar amount and a specified duration.

(2) The Federal savings association's performance under the agreement must create an authorized loan or other investment.

(3) The Federal savings association must treat its obligation under the agreement as a loan to the principal for purposes of §§ 560.93 and 563.43 of this chapter.

(4) The Federal savings association must take and maintain a perfected security interest in collateral sufficient to cover its total obligation under the agreement.

(c) What collateral is sufficient?

(1) The Federal savings association must take and maintain a perfected security interest in real estate or marketable securities equal to at least 110 percent of its obligation under the agreement, except as provided in paragraph (c)(2) of this section.

(i) If the collateral is real estate, the Federal savings association must establish the value by a signed appraisal or evaluation in accordance with Part 564 of this chapter. In determining the value of the collateral, the Federal savings

association must factor in the value of any existing senior mortgages, liens or other encumbrances on the property, except those held by the principal to the suretyship or guaranty agreement.

(ii) If the collateral is marketable securities, the Federal savings association must be authorized to invest in that security taken as collateral. The Federal savings association must ensure that the value of the security is 110 percent of the obligation at all times during the term of agreement.

(2) The Federal savings association may take and maintain a perfected security interest in collateral which is at all times equal to at least 100 percent of its obligation, if the collateral is:

(i) Cash;

(ii) Obligations of the United States or its agencies;

(iii) Obligations fully guaranteed by the United States or its agencies as to principal and interest; or

(iv) Notes, drafts, or bills of exchange or bankers' acceptances that are eligible for rediscount or purchase by a Federal Reserve Bank.

6. Section 560.3 is amended by revising the definitions of "Consumer loans" and "Home loans" to read as follows:

§ 560.3 Definitions.

* * * * *

Consumer loans include loans for personal, family, or household purposes and loans reasonably incident thereto, and may be made as either open-end or closed-end consumer credit (as defined at 12 CFR 226.2(a)(10) and (20)). Consumer loans do not include credit extended in connection with credit card loans, bona fide overdraft loans, and other loans that the savings association has designated as made under investment or lending authority other than section 5(c)(2)(D) of the HOLA.

* * * * *

Home loans include any loans made on the security of a home (including a dwelling unit in a multi-family residential property such as a condominium or a cooperative), combinations of homes and business property (i.e., a home used in part for business), farm residences, and combinations of farm residences and commercial farm real estate.

* * * * *

7. Section 560.50 is added to subpart A to read as follows:

§ 560.50 Letters of credit and other independent undertakings - authority.

A Federal savings association may issue letters of credit and may issue such other independent undertakings as are approved by OTS, subject to the restrictions in § 560.120.

8. Section 560.120 is amended by revising the first two sentences of paragraph (a) and paragraph (b)(2)(ii) to read as follows:

§ 560.120 Letters of credit and other independent undertakings to pay against documents.

(a) General Authority. A savings association may issue and commit to issue letters of credit within the scope of applicable laws or rules of practice recognized by law. It may also issue other independent undertakings within the scope of such laws or rules of practice recognized by law, that have been approved by OTS (approved undertaking).¹ * * *

(b) * * *

(2) * * *

(ii) In the event that the undertaking provides for automatic renewal, the terms for renewal should allow the savings association to make any necessary credit assessment prior to renewal;

* * * * *

PART 561 - DEFINITIONS

9. The authority citation for Part 561 continues to read as follows:

Authority: 12 U.S.C. 1462, 1462a, 1463, 1464, 1467a.

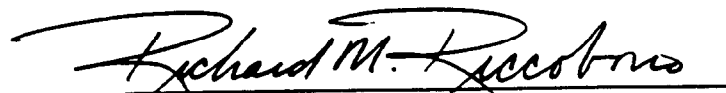
§§ 561.10, 561.11, 561.20, 561.21, 561.23, 561.25, 561.32, 561.36 [Removed]

¹ Samples of laws or rules of practice applicable to letters of credit and other independent undertakings include, but are not limited to: the applicable version of Article 5 of the Uniform Commercial Code (UCC) (1962, as amended 1990) or revised Article 5 of the UCC (as amended 1995) (available from West Publishing Co., 1/800/328-4880); the Uniform Customs and Practice for Documentary Credits (International Chamber of Commerce (ICC) Publication No. 500) (available from ICC Publishing, Inc., 212/206-1150); the United Nations Convention on Independent Guarantees and Standby Letters of Credit (adopted by the U.N. General Assembly in 1995 and signed by the U.S. in 1997) (available from the U.N. Commission on International Trade Law, 212/963-5353); and the Uniform Rules for Bank-to-Bank Reimbursements Under Documentary Credits (ICC Publication No. 525) (available from ICC Publishing, Inc., 212/206-1150).

10. Sections 561.10, 561.11, 561.20, 561.21, 561.23, 561.25, 561.32, and 561.36 are removed.

DATED: *AUGUST 19TH - 1999.*

By the Office of Thrift Supervision.


Richard M. Riccobono
Deputy Director